"Corporate Governance, Employee Welfare, and Firm Performance in Russia"

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ABSTRACT

This research analyses Russian industrial firms in the year 2000 with a focus on corporate governance (CG) in association with strategies relating to employee welfare and with firm performance. Privatised manufacturing industry in Russia represents a unique hybrid in terms of CG, with employees and managers as relational shareholders usually holding a majority of shares, but with an increasing proportion held by outsiders. While outside shareholders may be expected to promote strategies that raise shareholder value, other stakeholders introduce their own influences. Employees may seek higher wages, job security, social benefits, etc. in their roles as employees rather than shareholders. Managers may want income stability, continued employment, personal aggrandisement, growth of the firm, support in their political activities, etc. Thus, in a *Governance – Strategy – Performance* context, the following two research questions have been addressed: (1) do employees influence strategies concerning employee welfare and divert shareholder value towards their own immediate sources of welfare as employees and, subsequently, (2) are firms' strategic decisions concerning employee welfare associated with stronger or weaker performance?

The results obtained provide a rich basis for discussion on employee welfare in Russia. Being quite new at a general level, this work, as a large-sample empirical study, has been able to identify some important associations between insider ownership and strategies concerning employee welfare, and has discovered some interesting associations between employee-favouring behaviour in the firms and insider ownership. In terms of *Governance – Strategy*, workers' ownership was generally found to be positively associated with welfare provisions, while managers are mostly negatively associated with various forms of benefit and training provision for employees. In terms of *Strategy – Performance*, the results are rather mixed and do not permit simple conclusions, although they show possible improvement in the overall situation in Russia. The *Cost Minimisation* strategic cluster was found to be negatively associated with insider ownership. In terms of *Strategy – Performance* relations, only the new *Human Resource Investment* strategy is broadly associated with positive performance outcomes.

.....To my Grandad Alexander

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Long before this work was finished, I was thinking about the acknowledgements. How to write this part of my work, how to express my thanks to those who were guiding me, who have grown me and helped with my education, whom I met and whom I sorrowfully lost? This is the most pleasant task, but also the most difficult, for me.

This dissertation is the biggest achievement I have ever made in my research career, the result of years of studies and, I hope, a giant step forward in life.

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Abbreviations

ANOVA	Analysis of Variance
CEE	Central and Eastern Europe
CG	Corporate Governance
CIS	Commonwealth of Independent States
CJSC	Closed Joint Stock Company
CM	Cost Minimisation
EBO	Employee Buyout
EBRD	European Bank for Reconstruction and Development
EU	European Union
FCSM	Federal Commission for the Securities Market
FSU	Former Soviet Union
GDP	Gross Domestic Product
Goskomstat	State Committee of The Russian Federation on Statistics
HPWO	High Performance Work Organisation
HR	Human Resource
HRI	Human Resource Investment
HRM	Human Resource Management
IB	International Business
ILO	International Labour Organisation
IMF	International Monetary Fund
IO	Insiders' Ownership
JSC	Joint Stock Company
JV	Joint Venture
MBO	Managerial Buyout
MEBO	Managerial-Employee Buyout
MO	Managerial Ownership
MO^2	Quadratic Term of Managerial Ownership
MPP	Mass Privatisation Programme
OECD	Organisation for Economic Co-operation and Development
OJSC	Open Joint Stock Company

OLS	Ordinary Least Squares
RECEP	Russian-European Centre for Economic Policy
RF	Russian Federation
RIA	Russian Information Agency
SBS	Stolichniy Bank Sberezheniy
SEM	Structural Equation Model
SHRM	Strategic Human Resource Management
SITE	Stockholm Institute of Transition Economics
SM	Strategic Management
SO	State Ownership
SOE	State-Owned Enterprise
SPEC	Stanford Project on Emerging Companies
SSE	Sum of Squares due to Error
SSR	Sum of Squares due to Regression
SST	Total Sum of Squares
TSW	Traditional Social Welfare
USSR	Union of Soviet Social Republics
WO	Workers' Ownership (also referred to as employee ownership)

List of Variables

ABAW	Average Benefits for Administrative Workers
ABRW	Average Benefits for Regular Workers
CJSC	Closed Joint Stock Company
CM	Cost Minimisation
FI	Foreign Investment
HRI	Human Resource Investment
INCT	Increase in Training
IND	Industrial Sector Dummy
IO	Insiders' Ownership
IT	Initial Training
JSC	Joint Stock Company
LO	Layoff
MO	Managerial Ownership
MO^2	Quadratic Term of Managerial Ownership
OJSC	Open Joint Stock Company
PART	Partnership
PLE	Part of Larger Enterprise
SCSPC	Social Cost Share of Total Production Costs
SIZE	Logarithm of Absolute Number Employed
STATE	State Enterprise
TSPC	Training Share of Total Production Costs
TSW	Traditional Social Welfare
TU	Training to Upgrade
UL	Unpaid Leave
WO	Workers' Ownership
WSPC	Wage Share of Total Production Costs

CHAPTER I. Introduction and Background

This research analyses Russian industrial firms in the year 2000, and in particular focuses on their corporate governance (CG), on their strategies in relation to employee welfare and on firm performance. In this context, *governance/strategy/performance* studies in the West have been constrained by the relatively narrow range of governance structures prevailing. In contrast, the former Soviet Union (FSU) provides a rich research environment for empirical studies of actual (as opposed to hypothetical) CG, where employees as stakeholders in firms often have majority shareholdings. In addition, ownership shares are often disclosed in surveys by firms in the FSU in detail unavailable for Western firms.

CG has succeeded in attracting a good deal of public interest to corporations and societies in general. However, the concept of CG is usually indistinctly defined, as it potentially covers a large number of different economic phenomena. As a result, different researchers present diverse definitions that basically reflect their special interests. For instance, Goldberg and Desai (1999, p.42) define the term CG very broadly as "the entire system of rewards, sanctions, co-ordination and conflict-resolution mechanisms used to order and arbitrate the economic interests of shareholders, lenders, managers and employees". On the other hand, Shleifer and Vishny (1997, p.737) use CG in a narrow, shareholder-focused way and state that CG "deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment", and relate CG to financial instruments.

This thesis adopts the broad definition, proposed by the Organisation for Economic Co-operation and Development (OECD, 1999): "Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance". On this

definition, CG is broadly defined in terms of the firm's relationship with stakeholders and society, while elsewhere it is narrowly defined as the relationship of a company with its shareholders and other suppliers of finance.

Usually researchers distinguish two broad models of governance – the Anglo-American and European models, though Japan may be included in the latter. Anglo-American governance is characterised by dispersed ownership based on the liquidity and transparency of the stock market, with managerial decisions disciplined *indirectly* by share price movements. In contrast, with European governance, heavy external borrowing is combined with *direct* control and monitoring of investment decisions by lenders and other relational shareholders. The latter typically include banks, suppliers and competitors as shareholders, all with other relationships with the firms besides their shareholdings. In addition, other stakeholders (often without shares) may be represented on boards, e.g. employees.

Such governance variations have to be considered in terms of the prevailing political and business environment in each country when particularly being influenced by budget constraints, business crises at all levels and especially cross-cultural CG systems. It also has to be remembered that after the failure of the FSU with its command-administrative economy, system of ministries, life-time employment, extensive social welfare provisions, etc., post-1991 Russian enterprises have been heavily involved in corporate restructuring, changing the composition of the firm's assets and its corporate strategies at the same time. Arguably, the core idea of Russian market reformers and their Western advisers was to produce open capital markets, based on the Anglo-American model and a narrow concept of CG.

The give-away nature of the Russian mass privatisation programme (MPP) conveyed most property rights to enterprise insiders – managers and workers (Boycko *et al.*, 1995). In former socialist countries, privatisations that convey property rights to insiders are much easier to execute from a political point of view, as these programmes become politically more acceptable by the public. In this context, post-privatisation Russia's characteristics provide an interesting environment where managers and workers, as enterprise stakeholders, became major shareholders (Buck *et al.*, 1998; Frydman *et al.*, 1996a). In

other words, the Russian "giveaway" MPP produced an idiosyncratic form of ownership structure of "employee-owned, manager-controlled" firms (Earle and Estrin, 1996), which will be examined in more detail in Chapter II.

These circumstances raise two main groups of research questions, also discussed in detail in Chapter II, and addressed throughout this thesis: (a) as shareholders with an existing employee role within the firm, are managers or workers likely to divert shareholder value via human resource management (HRM) strategies towards their immediate sources of welfare (such as employment stability, wages, multiple social provisions), and, as a result, (b) are these strategies associated with stronger or weaker performance?

In studying the implied *Governance – Strategy – Performance* relationships underlying these questions, this thesis focuses on ownership proportions and legal company forms as two *governance* elements associated with HRM *strategy*, and ignores the overall company strategy or other governance influences, such as technology, etc. It has been argued (Linz, 1997) that the bulk of Russian manufacturing firms, that were part of the centralised ("mass") privatisation programme, have physical assets and products that are unsuited to global product markets. This implies that labour is the only consistently valuable asset in Russian enterprises, what gives a crucial role to HRM strategies as a means of maintaining, and hopefully enhancing, this stock of human capital. Thus, this research focuses on HRM *strategies* as a key bundle of strategy parameters, significantly associated with firm *performance*, with implications for the ability of Russian firms to compete globally. These *strategies* in particular include various forms of training, benefits, welfare provisions, etc., and ignore more general strategies, such as marketing. The notion of a strategic "bundle" refers in this thesis to practices, which are interrelated and internally consistent with respect to their impact on performance (MacDuffie, 1995).

To examine CG and HRM strategies in more detail, Western research is considered throughout Chapter III, the Literature Review and Hypotheses. In particular, the Strategic Management paradigm (*Governance – Strategy – Performance*) was adopted and justified for this Russian research, and particular HRM strategies, applied mostly in developed economies, were combined with strategies that are traditionally-specific for Russia.

Methodologically, the theoretical discussion in Chapter III suggests that the two main groups of research questions can be investigated using two types of statistical approach. The first uses correlation and regression analysis (OLS and LOGIT), while a second approach is based on the study of the three strategic HRM bundles, derived from Western theory. These bundles follow three broad alternative patterns of HRM strategies, identified here as: *Traditional Social Welfare (TSW)*, *Cost Minimisation (CM)*, and *Human Resource Investment (HRI)*.

We argue that the *TSW* strategy represents a continuation of initial founders' Soviet-style template of the employment relations, and thus, according to the privatisation outcome, could be supported by firm insiders, particularly by workers. The resulting performance is expected to be strong, though this strategy is recognised as involving short-term costs for the company. In contrast with *TSW*, *CM* represents a radical strategy for restoring control over cash flows via all possible cost reductions. Due to its potentially damaging psychological impact on employee welfare, *CM* is likely to be opposed by employees as employees, and consequently would not result in any performance improvements. The last considered strategy – *HRI* – is a high commitment HRM strategy that provides investments in employees with guarantees concerning employment stability and insurance provisions as a result of high commitments from both sides: the firm and its employees. Although it is recognised as "hard" HRM strategy, it is believed that this form of welfare provision will be associated with improved performance, achieved though more cost-saving strategy than *TSW*.

The theoretical discussion, presented in the Literature Review and Hypotheses Chapter, identifies important gaps in the literature in relation to the influences of *governance* on HRM *strategies*, and the consequences of these HRM *strategies* for firm *performance* in transition economies. We note that there has been no analysis of the inter-relations between *governance*, *strategies* and *performance* in Russia. Moreover, the three coherent HRM strategies (*TSW*, *CM* and *HRI*), interacting with various forms of share ownership inherited from the Russian privatisation programme, provide an extremely interesting laboratory for empirical research too. In this sense, the main objective of this thesis is to break new ground theoretically and empirically by studying employee welfare strategies in post-privatised Russia. It should also be noted that to date there was only one large-sample

empirical study by Buck *et al.* (2003) on the influence of governance forms on HRM strategies in the FSU, specifically Ukraine, and another research on *Strategy – Performance* examination of foreign subsidiaries operating in Russia, by Fey and Björkman (2001). Our research extends the Buck *et al.* (2003) and Fey and Björkman (2001) analyses by supplementing the *Strategy – Performance* approach of Fey and Björkman (2001) with a consideration of associations between *Governance – Strategy – Performance* on a sample of indigenous industrial Russian firms; and, compared with Buck *et al.* (2003), by studying the most developed State, founded after the collapse of the Soviet Union (EBRD, 2001), thus allowing to generalise the findings for the two FSU States afterwards. In addition, this study uses legal form governance variables, and alternative performance measures to the quantitative *capacity utilisation* and *sales per employee* measures used by Buck *et al.* (2003). Fey and Björkman (2001) argue the case for subjective measures of performance. Our research endorses their view and extends it by using negative measures of performance (e.g. perceived bankruptcy threat).

The choice of HRM practices, bundled together to produce the three HRM constructs, together with relevant statistical models, is presented in Chapter IV on Data and Methodology. Besides, as this Chapter's heading suggests, it also presents a discussion of the unique sample of data used in this research, survey methodology, and introduces the main independent and dependent variables, bundles of clusters, controls, and statistical models. The design and application of negative performance indicators, used for the first time in this kind of study, are a novel aspect of this research.

Subsequently, Chapter V on Results and Statistical Inference provides answers to the main research questions, examined via statistical testing of the hypothesised associations between *governance*, *strategy* and *performance* parameters. Without going into detail of these results here, this Chapter summarises the findings, that either support of oppose the hypothesised associations. The discussion of these results is provided in greater length in the concluding Chapter (Discussion and Future Work).

Finally, two Appendices – one presenting the questionnaire used for data collection, and another, providing details of cluster analysis – close this thesis.

CHAPTER II. Privatisations. Consequences and Associated Questions.

2.1 INTRODUCTION

Two governance systems can be said to have dominated the 20th century – capitalist and socialist. The socialist system persisted for quite a long, and still exists to some extent in the world's most populous county, China (Kornai, 2000). During this time, the socialist system has deeply influenced the realities, society, politics, economy, culture and life of people living in these countries. This is particularly true for all the now-independent states, created from the fifteen republics comprising the FSU, plus the countries of the East-European Socialist Bloc, and other developing economies, previously supported heavily but forced by the Soviet Union to implement the Russian model of management.

Following Kornai (2000), the model of the socialist system is characterised by a dominant state and quasi-state ownership, soft budget constraints, weak responsiveness to prices, plan bargaining and low quality of goods, a chronic shortage economy with vast state subsidies for poorly-performing sectors. In contrast, the capitalist (Western) system is characterised by the dominant position of private property, hard budget constraints, and strong responsiveness to prices. Countries changing from socialism to capitalism differ according to when these changes began, the economic and rational-choice prerequisites, and which path the country's economic advisors follow.

The Russian reform programme had four key elements: the elimination of price controls on most goods; the weakening of central planning for the supply, production and distribution systems; a focus on balancing the national budget and a start on the privatisation of state enterprises (Vlachoutsicos and Lawrence, 1996). With the main focus of this thesis on CG in Russian post-privatised firms, and a particular interest in questions concerning *Governance – Strategy* and subsequently *Strategy – Performance* mechanisms, we start this Chapter with a discussion on the History and Outcomes of Russian

Privatisation (Section 2.2), which ultimately informs the derivation of research questions and hypotheses.

It will be explained that privatised manufacturing industry in Russia represents a unique hybrid in terms of CG, with employees and managers as relational shareholders usually holding a majority of shares, but with an increasing proportion held by outsiders. It should be remembered however that there remains ambiguity over property rights, illiquidity of asset markets, ineffectiveness of bankruptcy laws, together with large shareholdings of banks in their role as strategic investors, typical of the European model. To look more closely on past studies of international privatisations of state-owned enterprise, Section 2.3 takes an insight into privatisations and CG models in the countries of Central and Eastern Europe.

Following the discussion on privatisations and their outcomes, Section 2.4 explores specific HRM policies, and identifies the most representative model for Russian manufacturing industry. This Section introduces a number of models, recognised in the Western literature, and argues the relevance of certain models for Russia-focused research. Following the discussion on privatisations and their implications for company employees, Section 2.5 defines the two main Research Questions which will be examined during this study. Section 2.6 concludes.

2.2 History and Outcomes of Russian Privatisation

The literature on privatisation identifies many motives. They include: improving the financial performance of state-owned enterprises (SOEs); raising finances for government spending; widening ownership through capital markets; improving service delivery; responding to pressures from external agencies (like the International Bank for Reconstruction and Development or the World Bank); replacing central planning with a market economy, etc. (De Castro *et al.*, 1996; Ernst & Young, 1992; Bishop and Thompson, 1993). However, in most cases the privatisation of SOEs represents a transfer of firm's ownership from the State (government) to private hands (Vickers and Yarrow,

1988). This has become an important tool of economic restructuring policies, especially in less-developed countries and former socialist regimes.

The first privatisation of SOEs dates from the policy initiative of the Thatcher Government in Britain in the early 1980s, and continued in many Western countries (like Japan, West Germany, Canada, etc.) in subsequent years. In the late 1980s many developing countries also made privatisation a part of their reforms (Young, 1987). The process continued through the 1990s, accelerated by the collapse of the socialist regimes in CEE, with subsequent transition towards free markets (De Castro *et al.*, 1996).

Following Estrin and Wright (1999), countries in transition may be divided into two groups. The first comprises countries of Central Europe, which have restored GDP and productivity growth, brought inflation under control and developed private sectors through privatisation. The second group includes much of the FSU's economies, which seldom achieved economic growth or control over inflation, and often appeared to have done little for enterprise restructuring. While the effectiveness and performance of privatised SOEs in CEE countries will be addressed in the next Section, this Section pays attention to privatisation reforms in the FSU, particularly Russia, in order to establish the theoretical basis for the subsequent analysis.

The Russian voucher mass privatisation programme (MPP), carried out between late 1992 and 1994 for most manufacturing firms, can be best described as insider privatisation which rapidly created the largest sector of insider-owned and controlled enterprises in almost any economy. In this period some 122,000 companies that produce up to 40% of GDP in Russia changed from State to private hands (Blasi *et al.*, 1997). According to the programme, every Russian citizen was granted a privatisation cheque – a voucher – that could be both invested in privatised enterprises at voucher auctions and traded. As a matter of fact, voucher privatisations in Eastern Europe and the FSU has attracted the greatest interest of researches and practitioners (see Boycko *et al.*, 1994).

Under the Russian MPP, the State offered three different scheme "variants" of privatisation for "large" enterprises – i.e. those with more than 1,000 employees and capital assets more than 50 million roubles on 1 January 1992. With the first variant,

employees were granted 25% of total shares and were also allowed to buy up to 10% of equity shares on preferential terms. Senior managers were granted 5% of equity, 29% was sold at voucher auctions and the remaining 31% remained in State hands, with a possibility of subsequent auction sales. With the third variant of MPP, 20% of equity shares were sold to those employees who took responsibility for enterprise restructuring. Another 20% were sold to all employees on preferential terms (at book value), 29% were sold at voucher auctions and the rest (31%) remained in State hands for subsequent auction. However, in most cases employees chose the second variant, giving them 51% of the shares on highly preferential terms (Blasi *et al.*, 1997; Boycko *et al.*, 1995). Only 29% of the capital of privatised companies was sold at voucher auctions, where employees and managers could increase their holdings up to 65% in 1994 (Blasi *et al.*, 1997). Remaining shares were retained by the State for subsequent auction.

Nevertheless, outside investors in the form of investment funds collected some of the vouchers and obtained 5.7% of the shares of privatised enterprises (Frydman *et al.*, 1996b). However, the regulation of voucher investment funds was generally weak, with low capital requirements, and no obligations for individuals to have financial qualifications and licences, so around 80% of 630 investment funds registered by 1994 were reported to belong to chief directors or managers of recently privatised enterprises. In subsequent years the shares left with the State were partially sold in auctions, mostly to management-affiliated companies or outside blockholders (Golubkov, 1999).

The choice of privatisation variant had to be approved by employees before 1 October 1992 by a simple 2/3^{rds} majority vote otherwise the first method was automatically applied. For small enterprises (with less than 200 employees or capital assets less than 1 million roubles) there was only one scheme of privatisation – sale at voucher or share auctions. All other enterprises that could not be identified as either large or small were able to choose between the three MPP variants and auction sale. Thus, 75% of large enterprises were privatised by the second variant of MPP, 24% by the first and only 1% by the third (Golubkov, 1999).

Also a lease-buyout method under the provision of the 1989 legislation was used outside the MPP. Leasing accounted for 25% of completed privatisations between 1993 and 1995

(Earle and Estrin, 1996). In this case, firms' assets, leased in 1990-1992, were acquired by employees at book value, and, as a result, insider ownership from the lease-buyout method was even higher than from the three MPP variants (Sprenger, 2002). Filatotchev *et al.* (1994) have criticised the ethics of redistribution through management buyouts. The authors argue that in buyouts of privatised SOEs, managers tended to receive all the rights of private entrepreneurs without many of the responsibilities, including the absence of a significant possibility of failure. Besides, the authors further argue that voucher schemes present problems involving the "divorce" of ownership and control in firms with diversified ownership, and that income redistribution in favour of managers and workers represents a huge expense for society. However, the Government did nothing to control the process (Black *et al.*, 2000).

The privatisation of nationally "strategic" firms from the military complex, transport, utilities, mineral extraction, oil, gas, telecommunications industries, etc. followed a different scenario, though a few primary producers were partly included in voucher privatisation. Among the most scandalous and criticised takeovers of the strategic enterprises was a loans-for-share scheme, elaborated and implemented by one of former Government vice premiers. By this scheme, five of the largest oil companies, monopolistic nickel producer Norilsk Nickel, and two metallurgy giants changed from State hands to private between 1995 and 1997, being firstly sold as part of a loans-for-share scheme with subsequent transfer of shares to affiliated commercial banks, as a guarantee for loans to the State budget. Once the Government defaulted on the loans later, the same banks bought these shares in non-transparent and poorly contested auctions (Johnson, 1997; Sprenger, 2002). However, the State still has controlling shares in many of the nationally "strategic" firms, like Unified Energy Systems or Gazprom (bundled into holding companies after the 1995-1997 privatisations), and in the defence-orientated industries.

Generally speaking, privatisation programs that convey property rights to enterprise insiders are much easier to execute from a political point of view, and in almost all transition economies, preferential treatment has been given to managers and workers in privatised enterprises to make these programs politically more acceptable. However, the resulting ownership proportions are difficult to calculate, at least in Russia. Offshore firms and holding companies provide vast opportunities for share dilution (accompanied by

extensive tax evasion), so it is almost impossible to identify both actual owners of the firms and the levels of profits. Nevertheless, Russian privatisation has favoured "insiders" (Boycko *et al.*, 1995), i.e. private ownership has mainly settled in the hands of managers and workers, or both. The term "insider ownership" applies to individuals or entities that own 10% or more of a company's shares. In this work, managers and workers together will be referred to as insiders, thus denoting that both types of owners are included, and the terms "worker" or "employee" will denote workers only.

Table 1 summarises available data on the distribution of ownership shares in Russian enterprises for a number of years.

Table 1. Estimates of the Ownership Structures (%) of Russian Industry (Various Surveys)

Ownership Structures	World Bank Survey [1] (1994)	Nottingham Survey [2] (1995/1996)	Blasi [3] (1996)	Russian Economic Barometer Survey [4] (1997)
INSIDERS	66.1	59.6	58	52.1
• Managers	19.6	14.0	18	15.1
• Workers	46.2	45.6	40	37.0
OUTSIDERS	18.9	29.3	32.1	38.8
• Individuals	5.9	6.5	6	13.9
• Non-Financial Firms	6.7	10.3	15.3	14.6
• Banks	1.0	1.5	1.6	0.9
• Investment Funds	4.5	4.6	5	4.3
• Foreigners	0.4	1.0	1.6	1.8
• Holding/Investment Companies	-	5.4	2.6	3.3
STATE	15.0	9.3	9	7.4
OTHERS	-	1.8	0.9	1.7
Total	100	100	100	100
Sample Size	235	314	357	135

Data sources: [1] Earle and Estrin (1996); [2] Filatotchev *et al.* (1999); [3] Blasi *et al.* (1997); [4] Aukutsionek *et al.* (1998)

According to the first – World Bank (1994) – survey, insider holdings after privatisation were as high as 66.1% of shares, divided between workers with 46.2% and managers with 19.6%, while all outsiders held only 18.9% of shares. In subsequent years, insiders' shareholdings decreased, as also did the State ownership. On the other hand, outsiders' ownership almost doubled within 1993-1997, and still continues to grow.

Among Russian insiders, managers are arguably the most powerful group, with their own share ownership and almost unlimited opportunities for hidden actions. Such hidden actions can include share dilution, self-dealing transactions in the form of asset stripping and transfer pricing, ability to pursue pet projects, delayed dividend payments, hiding of cash-flows from minority shareholders, workers, creditors, tax authorities and local governments, etc. If managers are linked to large stakeholders, they often use their power to expropriate minority shareholders, especially workers, who have more control over operational, work-related issues, than over strategic matter, and never reach a level of joint decision-making. Thus, managers are able to threaten workers with dismissals, decline in wages, cuts in the use of social facilities, etc., and may establish barriers to the selling of shares to outsiders (Sprenger, 2002).

The distinguishing feature of the Russian companies after the privatisation, that conveyed property rights to the insiders, was a large number of small owners. These owners, i.e. the shareholders, even though they have (ultimate) residual control rights in the form of votes, were too small and numerous to exercise this control on a day-to-day basis (Berle and Means, 1932). Therefore, they delegated day-to-day control to a board of directors (Filatotchev *et al.*, 1996a). In ideal circumstances, this board of directors would provide a check on management, ostensibly elected by shareholders to protect their interests. In some extreme cases, when shareholders are about to exhaust their trust to the managers, the board may replace the chief executive of the firm, or any other member of the management team (Hart, 1995).

However in the case of Russia, evidence suggests that although employees may have significant equity stakes, their involvement in boards of directors and other control mechanisms is generally very low (Filatotchev *et al.*, 1996a). Thus, the introduction of different forms of ownership and boards of directors has essentially delegated all control to managers. This has separated control and ownership and made workers representatives on boards rare or ineffective (Blasi and Shleifer, 1996). The resulting companies have been described as "employee-owned, manager-controlled" companies (Earle and Estrin, 1996), and the impact of employee ownership on strategic decisions may be weaker than expected from ownership proportions, since it is important to recognise and distinguish the difference between ownership and control. Nevertheless, managers are likely to be

influenced by employees to some extent, and this influence can be expected to vary with their holdings of shares.

The recent collapse of the FSU and the massive scale of Russia's indebtedness to the West arguably led to the "occupation" of Russia by Western creditors and economic advisors. These creditors were able to demand the most drastic political and economic changes, many reflecting US institutions of political democracy, company laws, capital markets and price liberalisation. Some of these regulatory changes, made partly under some Western influence and partly under the "new market economy" focus of the Government, had only temporal, weak or insignificant effect, and some had insidious and long term ones. Among these important and long term effects was foreign ownership in Russian enterprises, which accounted for 0.4% in 1994 (World Bank Survey), 1.0% in 1995 (Nottingham Survey), 1.6% in 1996 (Blasi) and 1.8% in 1997 (Russian Economic Barometer Survey). Although these levels may seem negligible (in comparison with the total of insiders' or outsiders' ownership for example), it has to be remembered that foreign ownership last existed before 1917.

Besides providing a weak regulatory environment for capital markets and share dealing, the generally weak role of the State as the outside owner within Russian privatised firms should be noted more specifically. Any State representatives on company boards are usually non-professionals and exercise little control. As shareholders, local governments take a position somewhere between insiders and outsiders, and are often very close to the management of the enterprises, providing some support to their decisions (Sprenger, 2002). Although usually the objectives of the State are not clearly identified, one of their main interests, however, is focused on the provision of public goods (e.g. social facilities) (Fox and Heller, 1999).

Initial ownership in many cases was not necessarily the most efficient one, because among the goals of privatisation program in Russia was a goal to complete privatisation quickly, so that all imperfections would be later corrected on secondary markets.

Since privatisation, workers' ownership has declined from 46.2% in 1994 to 31.5% in 1999, but still remains at a high level, while total outside ownership has increased from

18.9% to 42.4% (Kapelyushnikov, 2000). During the survey, conducted in 1999, ownership proportions for the year 2000 were predicted to reach 45.5% for insiders (with 18.2% hold by managers and 27.2% by workers), 44.9% for outsiders and drop down to 6.4% for the State. So, any expectations of a quick and dramatic sell-off by employees to outsiders, such as occurred for example in Japan in the post-war period (Aoki and Kim, 1995), did not occur. Nonetheless, Table 2 shows that insider ownership in Russia is falling over time, albeit slowly. Shifts in the ownership distribution have led to a gain in outside ownership, while workers and the State have lost.

Table 2. Estimated Ownership Distribution in Russian Industry, (%)

Ownership Structures	1995	1997	1999	2001[1]
INSIDERS	54.8	52.1	46.2	45.5
• Managers	11.2	15.1	14.7	18.2
• Workers	43.6	37.0	31.5	27.2
OUTSIDERS	35.2	38.8	42.4	44.9
• Non-Financial Outsiders	25.9	28.5	32.0	31.9
- Individuals	10.9	13.9	18.5	16.9
- Non-Financial Firms	15.0	14.6	13.5	13.5
• Financial Outsiders	9.3	10.3	10.4	13.0
STATE	9.1	7.4	7.1	6.4
OTHERS	0.9	1.6	4.3	3.2
Total	100	100	100	100
Sample Size	136	135	156	94

Data source: Russian Economic Barometer, 1995-1999 Surveys (Kapelyushnikov, 2000); [1] anticipated ownership during the 1999 survey.

According to Boycko *et al.* (1995), Russian privatisation has favoured insiders. This contrasts with some of the CEE countries (e.g. East Germany and Hungary), where direct sales and voucher privatisations to outside owners were predominant (De Castro *et al.*, 1996; EBRD, 1998; Estrin, 1994). Most analysts argue that the introduction of powerful

outside owners in Russia would have a positive influence upon enterprise CG, performance and restructuring (Earle and Estrin, 1997). In particular, this improvement is supposed to occur through improved monitoring of insiders, particularly of managers. However, despite all shifts in ownership within last years, it is clear that, on average, insiders are majority owners of Russian privatised manufacturing enterprises, where managers alone hold around the fifth of shares. Thus, the role of outside owners in insider-controlled firms may pose difficulties (Wright *et al.*, 1998a).

At the same time, outside owners brought new rules. In the Soviet era, firms (with no outside investors or owners) had many difficulties laying off workers, even for disciplinary reasons, but since transition began, this process has become easier. Now a reason for layoff could be a low skill level, low productivity or a disciplinary violation, although (Hoskisson *et al.*, 1994, p.1207) "...strategically laying off employees during times of economic stress" has also to be considered. Workers with low productivity or low skill levels could be easily replaced from the pool of unemployed. Among those who quitted voluntarily were typically those with the highest skills, who could receive significantly higher wages in the private sector. Mass layoffs occurred in the areas of technical support, in the social benefits sphere and in administration. It is therefore not surprising that among the unemployed are either the least productive workers or those with skills that are not in demand (Brown, 1998).

According to different surveys (Commander *et al.*, 1996; Dornbusch and Fisher, 1990; Russian Economic Barometer, 1996) managers often retain excess labour in the old Soviet style, hoping for an increase in demand and output. This seemed reasonable because firms could hoard workers since the expected costs of hiring replacement workers exceeded the benefit of layoffs. If firms released excess productive workers, then the cost of hiring productive workers from the pool of unemployed could fall to the level where releasing excess productive workers would be profitable, but unless hiring costs are generally high, firms could dismiss workers and hire them later, once production recovers (Brown, 1998).

Also it is recognised that employees with general-purpose skills and knowledge can leave the firm and be replaced without productive loss to either the worker or the firm (if efficient labour markets exist). Alternatively, employees with skills that are uniquely

tailored (specialised) to the requirements of the particular firm cannot leave without bearing substantial exit costs, and this fact often also stops managers from making mass layoffs.

Due to the high risk associated with a job change, most workers may now prefer to receive a lower wage paid reliably than to receive a higher wage from a firm whose stability is less clear (Brown, 1998). According to Morvant (1995), workers were owed eight trillion roubles ($1.8 billion) in unpaid wages. Any delay in payment together with double-digit inflation significantly reduces the real value of wages, and therefore workers may have looked for high risk premia during job change or preferred to stay with an old employer.

Employee ownership may therefore encourage excess labour retention and could be associated with workers' reluctance to shed labour. Since workers are relational shareholders, some conflict of interest may be expected, and may extend beyond labour retention to higher wages and to the social welfare policies of the firm in general. But workers in Russia often have little bargaining power and influence over wage and employment decisions (despite their dominant share ownership of the firm) and may accept cuts in real wages in just exchange for fewer layoffs (Wright *et al.*, 1998b). Besides, managers may wish to support many workers substantially, because firms with larger employment are more likely to receive State subsidies, so State support may be a powerful incentive for managers to promote employees' interests. However, high levels of labour hoarding and associated difficulties with accessing capital, slow restructuring, low levels of investment, etc. imply that one of the strategies to improve performance and find the way out of "business turnaround" situation could be cost-cutting and enterprise downsizing (in the short-term at least) (Filatotchev *et al.*, 2000).

This conclusion of Filatotchev *et al.* (2000) corresponds with a "hard" human resource management (HRM) strategy, identified in the Western literature as *Cost Minimisation (CM)* (Baron *et al.*, 1996; Beer and Nohria, 2000; Hannan *et al.*, 1996). This specific HRM strategy is characterised by extensive hiring/firing, instead of labour retention, with the aim to improve performance through cost reduction (Luthans and Sommer, 1999), to be described in Section 2.4 below, and then thoroughly examined in Chapter III of this thesis, together with two alternative HRM strategies. Here, we would only like to stress

that although *CM* could be introduced as the starting point for restructuring, employees (in their roles as employees rather than as shareholders) may feel that they will personally suffer from this strategy, and thus oppose it.

It was noted above, that the radical, *CM* strategy is recognised by Western theorists and practitioners, and was applied in a number of countries of the former CEE Socialist Bloc. The next Section provides a discussion of privatisation outcomes in a number of transition economies with some comparisons with Russia and the FSU countries.

2.3 Outcomes of Privatisations in Transition Economies

With the end of Communist regimes in Central and Eastern Europe, and transformation of the regions' economies, governments there began privatisation of SOEs in large numbers (Meyer, 2002; Uhlenbruck and De Castro, 2000). One of the major objectives of economic reforms in these countries was to increase the efficiency of production of formerly centrally-planned enterprises, making the output competitive on world markets (Filatotchev *et al.*, 2000). The reality, however, was different. Price liberalisation and the elimination of State control and central planning resulted in deep economic recession, accompanied by substantial investment declines in most of the countries, although theoretical perspectives of price liberalisation were quite the opposite (Blanchard *et al.*, 1993; Fisher and Gleb, 1991; Sachs, 1993).

Many CEE governments (such as Poland, the Czech Republic, etc.) opted to privatise their firms through the use of mass equity distribution among its employees, thus minimising social impact and public dissonance. However, one of the key issues in effective CG is the centralisation of ownership in outside hands. Thus, countries like East Germany and Hungary focused on wealth creation by selling SOEs to private investors, seen to be most likely to transform these enterprises into strong competitors (De Castro *et al.*, 1996; Freudenberg and Bird, 1991).

There is much evidence that firms from different countries tend to follow distinctive strategies, forced mostly by national institutional environments, which often predetermine strategic opportunities for business and limit the applicability of Western business strategies and organisational concepts (Erramilli, 1996; Hoskisson *et al.*, 2000; Kogut and Singh, 1988; Nohria and Garcia-Pont, 1991; Peng, 2000). This implies that strategies observed in transition economies are different from those in developed economies. Moreover, successful adaptation in one country does not necessarily imply that this strategy will be equally successful in another country or environment (Brewster, 2002).

Leaving a discussion of cultural differences beyond the research interests of this study, we nevertheless could provide a number of examples in support of the above statement. For instance, when organising country-specific aid programmes for developing economies, such powerful organisations as the International Monetary Fund (IMF) and Organisation for Economic Co-operation and Development (OECD) acknowledge the differences among countries (Licht, 2001). By doing this, these organisations try to prevent the implementation of a unique CG model worldwide, although they do not provide any guidance to how to distinguish country-specific environments – Russian versus Central European for example.

However, it was noted that properties of the old socialist system in modern CEE economies compare interestingly with Russia's characteristics, and echoes of the old system remain. In other words, "mentally" cultivated Soviet managerial practices and attitudes still exist to a considerable degree in many of CEE countries (Aguilar *et al.*, 1994) together with Soviet institutional embeddedness and strategic inertia (Gooderham *et al.*, 1999). For instance, in Hungary, which pioneered the market reforms in countries of the former Socialist Bloc, and where the transformation of state property to private hands has been achieved through a mass privatisation program (Stark, 2001; Stark and Bruszt, 1998), privately-owned firms still resemble the ministerial structures of former central planning system, with many of the old enterprise policies left (Stark and Bruszt, 1998).

After more than a decade in transition, Russia's economic performance is still disappointing when compared with such leading CEE economies as Poland, Hungary or the Czech Republic (Bevan *et al.*, 2001). In particular, the authors stress the lagging of

such major indicators of economic performance as life expectancy, enterprise restructuring, labour productivity, stabilisation of inflation and GDP growth. However, the economic and strategic implications of ownership changes and resulting performance are often still not clear, and there remains a considerable debate on the effects of privatisation on enterprise restructuring and performance that make such cross-country comparisons rather unreliable, if not misleading. For example, in a study of 61 companies from 18 countries (6 developing and 13 industrialised), privatised through initial public offerings, Megginson *et al.* (1994) show that most companies experienced increases in employment and sales after privatisation. In a later study of 85 full or partially privatised companies from 28 countries (13 developing and 15 industrialised) D'Souza and Megginson (1999) also show significant increases in profitability, real sales, operating efficiency and dividend payments. However, these studies were mostly based on enterprises from the financial sector (with only 30% manufacturing firms), and did not include any FSU firms, where public offerings of new shares were generally infeasible. Besides, among the enterprises studied, more than a third still had the State as a major shareholder, which could imply either hidden or open subsidisation (Filatotchev *et al.*, 2000). Thus, Megginson with his colleagues arguably gave misleading impressions of the impacts of privatisation in some transition economies (Filatotchev *et al.*, 2000).

Among other studies on privatisations in transition is Claessens *et al.* (1997), examining the cross-sectional determinants of performance improvements during 1992-1995 in a sample of 706 Czech firms involved in mass privatisation, 1991-1992. Using Tobin's Q[1] measure, the authors conclude that privatised firms do prosper, primarily because of concentrated ownership. Frydman *et al.* (1998, 1999) compare the performance of the Czech, Hungarian and Polish firms in a sample of 128 privatised and 90 state firms in the period between 1990 and 1993. The authors find that while average performance has increased after privatisation, the most significant increases in revenues and productivity occurred in firms privatised to outside owners. In addition, Pohl *et al.* (1997) compare the degree of restructuring achieved by over 6,300 state-owned and private enterprises in

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[1] Tobin's Q is the ratio of the market value of a firm's assets (as measured by the market value of its outstanding stock and debt) to the replacement cost of the firm's assets (Tobin, 1969).

seven CEE economies during 1992-1995, and conclude that privatisation increases the probability of restructuring and the probability of its success.

Spenner *et al.* (1998) researched Bulgarian SOEs. It is known, that Bulgaria resembled a smaller version of the Soviet economy during the Communist era, with almost a complete lack of political pluralism (Lampe, 1986). The first gradual Government reforms in 1990 were widely judged as a complete failure. The next – February 1991 "shock-therapy" reform, directed by the IMF and World Bank – included price liberalisation, trade policy reform, income policy reform, and fiscal and monetary policy reform. By 1993 this "shock-therapy" resulted in State crisis, substantial GDP decline, outstanding inflation and substantial unemployment – all major problems that Russia has been also faced with during the first years of privatisation. After examining the factors affecting the performance of Bulgarian SOEs during transition, Spenner *et al.* (1998) concluded that: (a) changes that had a market impact on performance were harmful if they involved core organisational changes, but, at the same time, (b) performance was significantly improving when these changes were consistent with environmental demands and did not require the development of new competencies and routines.

De Castro and Uhlenbruck (1997) examined how country characteristics affect *governance* and, in turn, firm *strategy*. More precisely, the authors studied 467 worldwide privatised firms in 1989-1992 with a particular interest in whether different country environments affect government approaches to privatisation, and whether country characteristics affect firm strategies. The findings suggest that there are differences for former Communist, less-developed and developed countries, and it is not possible to thoroughly generalise Western concepts across countries.

These results for CEE countries support the views of Erramilli, 1996; Hoskisson *et al.*, 2000; Kogut and Singh, 1988; Nohria and Garcia-Pont, 1991; and Peng, 2000, that firms from different countries tend to achieve different results (when applying distinctive strategies), caused mostly by different national institutional environments and limited ability to implement a unique CG model, even within Europe. Nevertheless, despite some ambiguity, in CEE there is evidence that the transformation of property rights away from the State to private hands results in shifts in performance, although often the origins of

these shifts are rather unclear. Thus, it has to be remembered that there are no universal solutions and ways out of "business turnaround" situations, and all restructuring policies and strategies have to be applied cautiously, taking into account country-specific environments and traditions.

This conclusion particularly applies to HRM strategies.

2.4 INTERNATIONAL AND RUSSIAN HRM STRATEGIES

A number of studies have described substantial differences in organisational structure, management and human resource policies between Western economies, CEE countries of the former Socialist Bloc, and Russia and the FSU (Filatotchev *et al.*, 1996; Uhlenbruck and De Castro, 2000).

Each country offers local idiosyncrasies in ways HRM is conducted. For example, American firms behave systematically differently from German or Japanese firms even though they compete on common global markets. The development of HRM strategies in the USA tends to be based on American individualism (Brewster, 1995, 2002; Guest, 1990), therefore, the US strategies do not thoroughly match the European or Russian reality.

A number of attempts have been made to identify country groupings within Europe. Gooderham *et al.* (1999) distinguish countries where the State has a limited role in industrial relations – UK, Ireland, Nordic countries, and countries where the State plays a key role in industrial relations – Roman-Germanic countries like Spain, France, Germany, Italy, Belgium, Netherlands and Greece. Hollingsworth and Boyer (1997) focus on the presence/absence of communitarian infrastructures in the form of trust, reciprocity, strong social bonds and co-operation among economic actors, essential for successful production.

The role of country-specific factors in HRM strategy were recognised by Porter (1990), arguing that the host county's environment is the main source of competitive advantage.

Later, Nelson (1993) and Soskice (1997) identified elements of countries' national innovation systems that assisted this process. Subsequently, many studies of differences across HRM strategies have used Hofstede's (1980, 1993) five cultural dimensions, that can be adopted here to examine the fit between Russian and Western HRM policies.

Hofstede's (1991) five dimensions in Russia show high *power distance*, high *uncertainty avoidance*, high *collectivism*, high *femininity* and high short-term orientation (Elenkov, 1998, Puffer and Shekshnia, 1996). Summarising Hofstede (1980), *power distance* indicates the extent to which society accepts that power in organisations and institutions is distributed unequally; *uncertainty avoidance* indicates the extent to which people feel threatened by uncertain and ambiguous situations; *collectivism* refers to a tight social framework where people distinguish between in-groups and out-groups, expecting their in-group (a firm, network or relatives) to look after them in exchange for loyalty to the group; and *femininity* refers to the value of caring for others, quality of life, and people.

In contrast with Russia, the United States has been characterised as having low *power distance*, low *uncertainty avoidance*, high *individualism*, high *masculinity*, and high short-term orientation (Hofstede, 1993), where *individualism* refers to people taking care of themselves and their families only (as opposed to *collectivism*), and *masculinity* refers to the extent to which assertiveness, money and things have dominant values for people (Hofstede, 1980).

These estimates of how Russia might rank on each cultural dimension and compare with the USA were later generally confirmed by Hofstede's (2003) recent estimates. These national cultural features may be argued to impact on national institutions and corporate strategies.

The strategic HRM literature generally supports the view that each firm should follow the type of the strategy that aligns with the primary business strategy (Sonnenfeld and Peiperl, 1988). According to an institutionalist perspective, organisational choice is limited by institutional pressure, including State and regulatory structures, interest groups, public opinions and norms (Oliver, 1991). Of course, the old FSU system involved various ministries mixed with regional authorities and top ("Soviet-style") firms' management

represented one of the most hierarchical and concrete forms of vertical control. This strict system of centrally-imposed vertical control in the FSU was also accompanied by Communist ethics, controlled by the Party leaders at all levels. Russia, as the main descendant of the FSU, is also generally viewed as a country that traditionally emphasises values of solidarity and close personal relationships (Elenkov, 1998; Stark and Bruszt, 1998), and where institutions seek to create security to reduce risks (Bollinger, 1994). This system may be expected to resist any attempts at reform in large industrial firms (Kornai, 2000), placing high priority on protecting past results rather than on taking risks in an uncertain future.

Labour management in the FSU was politically manipulated on a wide scale (Bendix, 1956) so official unemployment almost never existed and production levels were high. In particular, trade unions together with labour management were supporting all central HRM policies, which included tight work norms and subsequent individual performance payments, amounting to an extreme form of Taylorism, itself a variant on what has become known as the *Factory Model* in the Stanford Project on Emerging Companies (SPEC) literature (Baron *et al.*, 1996), discusses thoroughly in Section 3.3.

It has already been noted that Russia has generally been identified as having a national culture exhibiting high levels of collectivism (Elenkov, 1998), and thus a majority of firm-level social welfare provisions amounted to "high commitment" HRM policies Thus, employment relationships were effectively based on lifetime employment and enterprises provided many of the social needs of both current and retired employees. The range of these benefits and other Soviet-style HRM provisions will be described below, and is referred to here as a *Traditional Social Welfare (TSW)* strategy. Here it should be noted that this *TSW* strategy corresponds with the paternalistic HR strategy in some British industrial firms in the 19th Century, but which has by now become a rather unfashionable business strategy in the West (Wray, 1996). Today, *TSW* slowly becomes old-fashioned for Russia too, where many of joint ventures of Western investors do not provide traditional Soviet-style welfare provisions for employees, mainly because firms cannot afford this costly form of HR commitment. However in some CEE economies (e.g. Bulgaria) *TSW* still exists, providing employees with job security and signalling a long-standing commitment to their workforce (Spenner *et al.*, 1998).

Of course, high-commitment work practices and social welfare provisions are also a feature of many Asian, especially Japanese, firms, though it is unclear whether the resulting system on balance benefits employees or exploits them. For example, Japanese HRM has been praised as comprising paternalistic, non-calculative, team-based relations (Gooderham et al., 1998), while elsewhere an allegedly darker side to lean production, continuous improvement, quality circles, etc, has been identified (Legge, 1995).

Following the outcome of the Russian MPP, that conveyed most property rights to enterprise insiders, and taking into account the fact that paternalism towards workers was generally a consistent feature of enterprise behaviour in the context of the FSU, we will be considering non-Western *Traditional Social Welfare* as one of the main HRM strategies for Russian post-privatised privately-owned industrial firms, related to enterprise wellbeing in Russia, and resulting in improved performance. (It must also be remembered that substantial welfare provisions to company employees also implies costs for shareholders.)

At the same time, Western literature in nowadays is concentrated on HRM strategies, different from those described by the *Factory Model* or corresponding to the *TSW* template. The question of identification of these specific HRM practices confronts most Western HRM research, including studies by Baron *et al.* (1996, 1999), Hannan *et al.* (1996), MacDuffie (1995), Osterman (1999, 2000), Spenner *et al.* (1998), etc. Besides the *Factory Model* explained already, these authors also introduce the *Autocracy*, *Bureaucracy*, *Commitment*, *Engineering* and *Star Models* (see Section 3.3 for a formal description of these models). Some of them are quite distinctive in presenting business strategies and the resulting methods of employee relations, others are much alike.

A discussion below (see Section 3.3) provides a comparison between the models, presented by Baron *et al.* (1996, 1999), Hannan *et al.* (1996), MacDuffie (1995), Osterman (1999, 2000), and Spenner *et al.* (1998), and others used in the FSU, for example, by Buck *et al.* (2003) or Fey and Björkman (2001). As a result of this discussion, two other distinctive HRM strategic models – *Cost Minimisation (CM)* and *Human Resource Investment (HRI)* – have been chosen to represent the key HRM strategies for this *Governance – Strategy – Performance* study of Russian enterprises.

The *CM* strategy has been already briefly introduced in Section 2.2 above as radical ("hard") HRM strategy, departing most decisively from the antecedent traditional Soviet-style *TSW* , and designed to improve performance through cost reduction (Luthans and Sommer, 1999). Besides the *Autocracy* or *Bureaucracy Models* (Baron *et al.*, 1999) and the *Factory Model* (Baron *et al.*, 1996; Hannan *et al.*, 1996), Western literature also identifies a *CM* strategy as "Theory E" (Beer and Nohria, 2000). Following these authors, *CM* is common among restructuring US companies (in particular, it was examined in high technology US firms), where it is focused on the maximisation of shareholder value and is achieved through financial incentives mostly.

For Russian national culture and philosophy, this strategy is fairly likely to result in reduced performance as it does not resemble established views on welfare provision, and thus considered by company employees to be damaging. As shareholders, employees could win, but as employees they are more likely to lose, as found to be in Ukraine (Buck *et al.*, 2003).

The third recognised HRM strategy for Russia is *Human Resource Investment*, which itself is quite different to *TSW*, but, as opposed to *CM*, involves high commitment investments in employees with the purpose of raising performance and productivity in an attempt to establish a "psychological contract" between workers and their firms (Guest, 1998). This HRM strategy is identified by Baron *et al.* (1996, 1999), Hannan *et al.* (1996), MacDuffie (1995), Osterman (1999, 2000) as the high *Commitment Model*, or as "Theory O" by Beer and Nohria (2000).

According to *HRI*, employees are provided with informal guarantees concerning employment stability, training, education, provision of benefits in exchange for their commitment to the enterprises, i.e. pay as fair exchange. While the social contracts theory of business ethics, proposed by Donaldson and Dunfee (1994), recognises the difference between cultures accepting corporate paternalism (like Russian) and cultures with highly individualistic, non-paternalistic beliefs (e.g. American), recent studies by Buck *et al.* (2003) and Fey and Björkman (2001) empirically support the theoretical expectation of strong efficiency gains from high-commitment "psychological contracts" for enterprise performance, and suggest that, although being recognised as a Western HR strategy, *HRI*

could result in productivity, quality and performance gains in post-privatised enterprises of the FSU.

High-involvement HRM strategies (like *HRI*) start with management philosophies and core values that emphasise the significance of employees as a source of competitive advantage (Bae and Lawler, 2000). To develop this resource, close cooperation between Russian managers and other enterprise employees is needed. As was noted in Section 2.2, to large extent this closeness was itself reflected in the 1992 privatisation schemes of the Russian Government, which gave priority to workers' rights of ownership and representation (Blasi and Kruse, 1992).

This suggests two main sets of research questions, one that addresses *Governance – Strategy* relations, and another that is concerned with whether the *strategies* chosen are indeed associated with costs or benefits in terms of *performance* outcomes. To examine these relations, the next Section addresses the Research Questions.

2.5 Research Questions

The above discussion presented an introduction to privatisation in Russia, and in some FSU and Central and East-European countries. It was noted that, after the collapse of the Soviet Union, a Russian mass privatisation programme (MPP) using vouchers, carried out for most manufacturing firms between 1992 and 1994, produced an idiosyncratic form of ownership structure of "employee-owned, manager-controlled" firms (Earle and Estrin, 1996). This outcome to large extent resulted from the give-away nature of the MPP, which conveyed most property rights to enterprise insiders – managers and workers (Boycko *et al.*, 1995). The reason why the Russian Government decided to distribute State property through equity allocation among its employees was more politically rather than economically driven.

Some of the CEE economies also followed this path of equity distribution during their SOE privatisations (e.g. Poland or the Czech Republic). Other countries (like East

Germany or Hungary) focused on wealth-creating methods of privatisation, and started selling their SOEs to potential outside investors (De Castro *et al.*, 1996; EBRD, 1998; Estrin, 1994; Freudenberg and Bird, 1991). They recognised that privatisation to outsiders represented opportunities to achieve increases in revenues and productivity, as it has occurred in Czech, Hungarian and Polish privatised firms (Frydman *et al.*, 1998, 1999).

For Russia, most analysts also argue that the introduction of powerful outside owners could have a positive influence upon enterprise CG, performance and restructuring (Earle and Estrin, 1997). However, it has to be remembered that one of the initial goals was to complete privatisation quickly, so that all imperfections would be later corrected on secondary markets: recent changes in ownership proportions suggest (see Tables 1 and 2), that total outside ownership was increasing during recent years, while the total of insiders' has declined (though, at the same time, managers' shareholdings were increasing) (Kapelyushnikov, 2000).

It was noted that *strategies* in transition economies vary a lot, being often heavily influenced by a need for social legitimacy; diverse national cultures and business systems; institutional and legislative factors; managerial development and career structures, the degree of competence of HR specialists, etc. While outside shareholders may usually be expected to promote strategies that raise shareholder value and nothing else, other stakeholders may introduce their own influences. For example, workers may seek higher wages, job security, social benefits, etc. (in their roles as employees rather than as shareholders), and managers may want income stability, continued employment, personal aggrandisement, growth of the firm, support in their political activities, etc. (possibly at the expense of shareholder value).

Among other studies on possible forms of association between *governance*, *strategies*, and *performance* in the FSU, CEE and other transition economies, this thesis extends the singular Russian *Strategy – Performance* analysis of Fey and Björkman (2001), with a consideration of the associations between CG – in the form of corporate ownership structures and legal company forms – and different HRM strategies. In particular, by addressing *Governance – Strategy* relations in Russian "employee-owned, manager-controlled" post-privatised firms, we are interested if the opportunistic concerns of

employee-owners prevail over shareholder value, i.e. do employees influence *strategies* concerning employee welfare and divert shareholder value towards their own immediate sources of welfare as employees? Subsequently, another concern of this study is represented by the second research question on whether the chosen *strategies* are indeed associated with costs or benefits in terms of *performance* outcomes, i.e. with stronger or weaker performance.

To summarise, the two main groups of research questions will be addressed concerning:

(a) *Governance – Strategies*. Through their influence on managerial strategic decisions, does employee ownership influence strategies concerning employee welfare, and divert shareholder value towards their own immediate sources of welfare as employee (employment, wages, social benefits, etc.)?

(b) *Strategies – Performance*. Subsequently, are firms' strategic decisions, directed to some extent at short-term employee welfare, associated with stronger or weaker performance? As a mirror-image of this question, are employees as shareholders associated with shareholder value?

These two main groups of questions will be examined during the remainder of this thesis within two types of approach used for this research. The first approach uses correlation and regression analysis (OLS and LOGIT) for testing the two main hypotheses, formulated for *Governance – Strategy* and *Strategy – Performance* research in Section 3.2 below. The second approach is based on the study of the three strategic HRM bundles, derived below from Western theory, and representing *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* strategies. However, before these research questions are addressed, a suitable theoretical lens (or lenses) must be chosen and justified for this Russian research.

2.6 CONCLUSION

The question of associations between *Governance – Strategy – Performance* in terms of employee welfare in Russian industrial firms opens another field for analysis of post-privatised economies. It has to be recognised that this analysis will require different methodology and techniques, which will be described in later chapters.

Nevertheless, numerous findings on the outcomes of privatisations in Central and Eastern Europe and some of the FSU countries, presented in this Chapter, suggest that there are both similarities and differences among countries which prevent the direct application of established CG models and strategies, successful in one places, to another. In particular, these differences include diverse national cultures and business systems; institutional and legislative factors; managerial development and career structures, and the degree of competence of HR actors, etc.

Post-privatisation Russia, as a descendant of the Soviet Union with its strong history of hierarchical ministries in a command-administrative economy, a highly integrated industrial structure and soft budget constraints, inherited a system that reduced many uncertainties for managers (but increased others), was highly centralised with strong collectivistic attributes and possessed a lack of experiences of the West and market economies (Ennew *et al.*, 1993). Following the above discussion, the resulting ownership structure of Russian enterprises, described as "employee-owned, manager-controlled" (Earle and Estrin, 1996), could influence strategic decisions in favour of employees' immediate sources of welfare – job stability, high wages, social benefits, etc. This implies that such a non-strategic concern for employee-owners, perhaps being less focused on raising shareholders' value, than on welfare provisions for themselves, could be damaging to a firm's financial performance. These possible influences of employee-owners on company *strategies* and subsequent *performance* of the enterprises set up the two main research questions of this study.

It is also worth noting that this thesis focuses on ownership proportions and legal company forms as two *governance* elements, associated with *strategy*, and ignores the overall

company strategy or other governance dimensions like technology, etc. Besides, the only *strategy* parameters, associated with firm *performance*, are HRM strategies (training, benefits provision, etc.), ignoring marketing strategy for example, and other general firm strategies.

There is also a growing debate on which HRM model to adopt for successful performance. Chapter II presented three major HRM strategies (models), identified in Western literature, and adopted in some of transition economies. More precisely, Chapter provides examples of two cost-effective strategies – either *Cost Minimisation* or *Human Resource Investment* – and another, reflecting the Soviet founders' employment template, recognised as the *Traditional Social Welfare* strategy. To check for interactions between *governance* and *performance*, these three coherent strategies will be accommodated for Russian firms by a cluster approach, developed in the review of relevant HRM literature, presented in Chapter III of this study.

Thus, the structure and ownership concentration in Russian firms raises a number of questions in relation to *Governance – Strategy – Performance* that are important for theory and policy. What are the HRM strategic clusters that best characterise Russian alternatives, what *governance* is associated with these strategic clusters and are the different *strategies* associated with significantly strong or weak *performance*? This thesis is intended to provide answers to these questions.

CHAPTER III. Literature Review and Hypotheses

3.1 INTRODUCTION

This Chapter presents a literature review relevant to the analysis of CG in Russian post-privatised firms, with a particular focus on questions concerning *Governance – Strategy* links and subsequently *Strategy – Performance* mechanisms, leading to relevant hypotheses. It proposes a stakeholder perspective for the analysis of large privatised firms in Russia and develops testable hypotheses in relation to HRM strategy bundles derived from Western theory.

The break-up of the FSU after 1991 and subsequent policies promoting global integration and mass privatisation, leading to employee-owned businesses as the dominant form of governance in manufacturing industry in Russia, Ukraine and Belarus have already been described (Filatotchev *et al.*, 2000; Hoskisson *et al.*, 2000). To date, however, there has been only one large-sample empirical study of the influence of governance forms on HRM strategies (in Ukraine, see Buck *et al.*, 2003), and only one (Fey and Björkman, 2001) on the consequences of these strategies, for firm performance, in Russia in 1998. However, the Fey and Björkman (2001) study only investigated relationships in foreign-owned subsidiaries (Finnish, Swedish, US, German and British) in Russia, located in just two cities (Moscow and St. Petersburg), and did not cover any indigenous Russian enterprises.

This research focuses on indigenous Russian firms and extends the Fey and Björkman (2001) and Buck *et al.* (2003) analyses in a number of ways. In the context of a mass privatisation programme that conveyed most property rights to insiders, it completes the established *Governance – Strategy – Performance* sequence (Hitt *et al.*, 1996; Thomas and Waring, 1999), by supplementing the *Strategy – Performance* approach of Fey and Björkman (2001) with a consideration of associations between corporate governance – corporate ownership structures and the legal forms of enterprises – and different HRM strategies. Compared with Buck *et al.* (2003), this study, firstly, represents an advance in terms of studying Russia – the most developed State, founded after the collapse of the

Soviet Union (EBRD, 2001). It is well-known that Ukrainian market reforms are weaker than Russia's, thus Russian firms could be more generous in the extent to which they are ready to provide social facilities and benefits to its employees, thus reducing any bias towards cost-cutting strategies. Secondly, by supplementing the Buck *et al.* (2003) Ukrainian study with the analysis of *Governance – Strategy – Performance* in Russian industrial firms, it will be possible to generalise the findings. However, unlike Buck *et al.* (2003), this thesis does not address research questions with Structural Equation Model (SEM) techniques. SEM analysis methods have serious weaknesses, and it was thus decided not to use these techniques for this study. (These limitations will be addressed in Chapter IV below). The approach here also embraces legal forms as a governance element in addition to the ownership variables; and alternative performance measures to the quantitative capacity utilisation and sales per employee variables, used by Buck *et al.* (2003).

In terms of the stakeholder approach proposed below, the circumstances in Russia provide an interesting environment where managers and workers, as enterprise stakeholders, became major shareholders and board representatives. As shareholders with an existing employee role within the firm, are managers and other employees likely to divert shareholder value towards their immediate sources of welfare such as employment stability, wages, multiple social provisions, and are these decisions subsequently associated with stronger or weaker performance?

To answer these questions in the context of the proposed research, the next three main sections (with a number of subsections) review those theories, developed in relation to Western organisations, that could be appropriate for Russian firms as well, and focus on relevant HRM theories in order to address the research questions and develop hypotheses. Besides, these three main sections provide a theoretical ground for two types of analyses, applied for this thesis – (a) correlation/regression analysis and (b) cluster analysis with three coherent HRM constructs.

More specifically, Section 3.2 justifies The Choice of Paradigm and introduces two main hypotheses for:

- 3.2.1 *Governance – Strategy* relationships, and

- 3.2.2 *Strategy – Performance* mechanisms.

Then, Section 3.3 introduces a review and formulates relevant hypotheses for HRM Theory and Strategic Clusters, and focuses on:

- 3.3.1 *Traditional Social Welfare* Strategy,
- 3.3.2 *Cost Minimisation* Strategy,
- 3.3.3 *Human Resource Investment* Strategy, and
- 3.3.4 Mixed HRM Strategies and Summary on Appropriate Clusters for Russian Research.

Finally, Section 3.4 concludes.

3.2 THE CHOICE OF PARADIGM

3.2.1 GOVERNANCE – STRATEGY

To fill the gap in analysing *Governance – Strategy – Performance* link in Russia, the Strategic Management (SM) paradigm is adopted here to address the research questions set out in Section 2.5. The adoption of an analytical structure developed within the SM paradigm in general, and within Stakeholder Analysis in particular, provides an important framework of analysis. In general, the SM approach has established a sequence of *Governance – Strategy – Performance* (Hitt *et al.*, 1996; Thomas and Waring, 1999), with subsequent *Performance – Governance* feedback, developed mainly in the context of strategic decisions concerning diversification (Hoskisson and Turk, 1990).

The following picture presents a framework of model, which is to be tested in this study:

In this thesis, the relevant strategies are human resource strategies. It is recognised that the specific strategy relating to employee welfare within firms (wage levels, job creation,

spending on training, health insurance and on other social provisions) has a long tradition within other literatures. Indeed the intention here is to synthesise these different perspectives under the SM umbrella.

For example, within the Human Relations tradition, there is a substantial literature on "social contracts" and on "welfare capitalism" (e.g. Jacoby, 1997). This literature provides useful insights for the subject at hand. For example it distinguishes an era of enterprise-driven welfare provision in the US (approximately 1880–1950), that contrasts with the typical European welfare state, where most of the burden of welfare provision was transferred from the enterprise to the State. From this perspective, the Soviet period can be seen as an interesting intermediate case, typically mixing substantial amounts of enterprise-level welfare provision in the form of housing, kindergartens and polyclinics, etc., backed up by considerable State support in the form of subsidised household materials and services, minimum wage legislation, etc.

Similarly, the Occupational Psychology literature has focused on the "psychological contract" whereby the firm implicitly provides employees with informal guarantees concerning employment stability and discretionary insurance provisions. In return, the employee may contribute effort on behalf of the firm that exceeds any contractual obligations and increase firm performance (see a whole special issue of the *Journal of Organisational Behavior*, particularly Guest, 1998). This perspective provides a useful antidote to the notion that most spending on employee welfare in some sense "wastes" shareholder value and threatens the survival of firms that must compete on global markets (Greenaway and Nelson, 2000). Further support for this antidote is provided by the UK Government's White Paper in December 2000 on Globalisation and Poverty.

This research synthesises these different literatures with the view that major HRM decisions by the firm are crucial to the development of a firm's human capital, a key enterprise capability in a resource-based view of the firm. As with the psychological contract, a resource-based view emphasises the positive aspect of those investments in employees that produce a resource that is unique, value-creating, and hard to imitate by competitors (Barney, 1986, 1991, 1995). Alternatively, employees may demand investment in their own human resources at a level that reduces firm value, and, in a

competitive market economy, such firms may be out-competed by firms that employ "flexible production" and the casualisation of employment relations (Birkenshaw and Hagström, 2000; Kleinknecht, 1998; Wood and De Menezes, 1998), leaving social provisions (e.g. employment insurance, holiday entitlements and pensions) to the individual worker's personal resources. However, strategies which include the flexible recruitment and optional retention of workers for particular tasks are generally opposed by a majority of Russian employees, as not conforming to their national culture and psychology of high uncertainty avoidance and thus enhanced employment security (Elenkov, 1997, 1998).

It must be admitted, however, that, in addressing these issues, the SM literature has typically paid little attention to the determination and consequences of strategic decisions concerning employee welfare. Significant exceptions would include studies of strategies concerning the consequences for employment change of major shifts in company ownership/governance (e.g. Johnson, 1996, on MBOs; and Lichtenberg and Siegel, 1990, on the impact of post-takeover restructuring).

Stakeholder Theory (see a whole number of the *Academy of Management Journal*, particularly Berman *et al.*, 1999) has been advanced and justified in the management literature due to its instrumental power, descriptive accuracy and normative validity (Donaldson and Preston, 1995), but has been generally concerned with the influence of different stakeholders (besides dispersed outside shareholders) on strategic decisions in general, but with no specific concern for employee welfare. It is proposed that for the purpose of this thesis, a consideration of the effect and importance of different stakeholders can provide the basis for the analysis of stakeholder influence over HR strategies and subsequent firm performance.

Donaldson and Preston (1995) describe the different approaches of Stakeholder Theory. Firstly, it can be descriptive, and "presents a model describing what the corporation is". Secondly, it may be instrumental, i.e. it establishes a framework for examining the connections between the stakeholder management and the achievement of corporate performance goals, measured conventionally through growth, firm stability, profits, etc. Thirdly, Stakeholder Theory can be managerial, recommending structures, attitudes and

practices, that "taken together constitute stakeholder management" (Donaldson and Preston, 1995).

Whatever the particular approach, Stakeholder Theory defines "stakeholder" as any individual or group of constituents, who can affect or is affected by the achievement of the firm's objectives (Freeman, 1994), or have a legitimate claim on the company (Pearce, 1982), where this legitimacy is based on the existence of a reciprocal relationship. The term stakeholder usually embraces stockholders, managers, employees (workers), creditors, customers, suppliers, local authorities and the general public (Hill and Jones, 1992), and includes primary and secondary stakeholders. Primary stakeholders include shareholders, managers, employees, consumers and local authorities. The State and civil institutions usually constitute secondary stakeholders, although the State can be a primary stakeholder too, through direct ownership of the firm.

Following March and Simon (1958), participants (stakeholders) supply their own contributions to the firm and, in exchange for these contributions, expect fulfilment of their interests (through rewards and influence). Stockholders, as a particular subset of stakeholders, possess capital, which they are ready to invest in exchange for certain returns. Loans from creditors provide the firm with funding, and are expected to be paid back in time, with interest. Managers and workers work for "fair" wages and decent treatment (e.g. welfare provision, good working conditions and other benefits), providing firms with their skills and human capital. Suppliers provide the firm with various inputs, that turn later into saleable products, which customers are ready to buy (for fair prices) in exchange for their money. Local authorities provide an infrastructure and expect loyalty from citizens (Hill and Jones, 1992).

The stakeholder approach argues that all individuals or groups contribute to an enterprise in order to receive benefits. Thus, shareholders try to maximise the value of the firm; managers may want to maximise the size of the firm; employees may favour strategies that raise their wages and secure jobs; the State may seek to raise votes through job preservation; banks may support actions that secure company liquidity, etc. However, both the finance and SM literature, as well as agency theory, have noted the existence of a variety of agency conflicts within modern firms (Jensen and Meckling, 1976).

These agency conflicts generally refer to shareholders and managers, but also arise in relation to managerial behaviour with respect to each class of stakeholders, and particularly workers. At present, scholars note quite a weak role for shareholders and banks within Russian firms, some weak (generally subordinate) influence for workers, and a dominant role for managers (Buck *et al.*, 1998). Also Hill and Jones (1992) assert that the stake of an individual (unskilled) worker, especially with few alternative employment opportunities, is likely to be negligible, e.g. in many Russian cities.

This raises the question of stakeholder identification and salience – the degree to which managers give priority to particular stakeholders' claims (Mitchell *et al.*, 1997), a concept that is very close to the concept of resource dependency (Pfeffer and Salancik, 1978). In the salience literature, there is no normative discussion of whether managers *should* pay more attention to a particular group of stakeholders. However managers often do pay more attention to some certain kinds of stakeholders as a result of their bargaining power and ownership of key resources that the firm needs, causing the described agency conflict. Kotter and Heskett (1992) propose that managers care strongly about people who have a stake in the business – customers, employees, stockholders, suppliers, etc. In this situation workers, particularly as shareholders, should have a legal and moral claim on the firm and an ability to influence the firm's behaviour. However, as already noted, employees in Russia have little bargaining power over managerial decisions because of limited alternative employment opportunities and their dependence on the firm for many social provisions, e.g. housing. This diminishes the salience of employee stakeholders.

One possible way of resolving powerful stakeholder influence and subsequent agency conflict involves the takeover mechanism, which depends upon the ease of buying/selling shares (shareholder "exit") on a capital market and disciplines management by easy replacement procedures (Driver and Thompson, 2002). However, according to these authors, regardless of the threat of a possible takeover, empirical evidence is "against the view that actual takeovers are primarily aimed at correcting or eliminating poor management" (p.113).

As an alternative to the discipline of capital markets, a stakeholder approach may lead to the building of good relations with stakeholders – employees, buyers, suppliers, creditors,

local communities, etc., which could lead to competitive advantage if these stakeholders apply effective monitoring of managers (Hillman and Keim, 2001). Hillman and Keim (2001) test this proposition with 500 *Standard & Poor's* listed firms and find that stakeholder management leads to improved stakeholder value, while from the social side this association is negative.

In contrast with Stakeholder Theory, one branch of the law literature stresses the principle that boards and corporate managers in particular should act exclusively in the economic interests of shareholders (Hansmann and Kraakman, 2002). While national and international government officials continue to debate on effective CG mechanisms that will deliver managerial accountability and accompanying efficiency increases (Wright *et al.*, 2003), Hansmann and Kraakman (2002) suggest that the standard legal model of the corporation results partly from the failure of alternative models, such as the manager-focused US model, the labour-focused German model, and State-focused model, recently dominant in France and most of Asia. As a result of the development of this new kind of model, the efficiency and performance of a company is expected to improve. However, recent findings also emphasize institutional differences in governance, share ownership and local business culture among Europe, US and other countries (e.g. see Gilson and Roe, 1993; Roe, 1993).

In the case of Russia, there has been an examination of the effect of outside investors on CG in Russia (Earle *et al.*, 1996; Frydman *et al.*, 1996a,b), while attention towards other important stakeholders, particularly managers and workers, has been less extensive. Nevertheless, some findings suggest that even though employees have significant equity stakes in their own enterprises, their involvement in boards of directors and other control mechanisms is generally very low (Filatotchev *et al.*, 1996a; Hansmann and Kraakman, 2002), and ineffective (Blasi and Shleifer, 1996).

Focusing on shareholders as dominant stakeholders, another important issue within a *Governance – Strategy* framework is the question of the influence of ownership structures on firms' strategic decisions. The core idea of Russian market reformers and their Western advisers was to produce open capital markets, based on the Anglo-American "exit" model. Following Buck *et al.* (1998) and Frydman *et al.* (1996a), the market reforms and

manager-employee "giveaway" privatisations in Russia have secured the presence of these two groups of enterprise stakeholders, and also used their voice to prevent a withdrawal of the State from the governance of industrial enterprises, though the aim of privatisation was to remove State influence too.

As may be expected from their low salience, the evidence suggests that employee involvement in strategic decisions and other control mechanisms is generally very low in Russia (Filatotchev *et al.*, 1996a), and managers are able to threaten workers into submission with dismissals, wage cuts, etc. (Sprenger, 2002). In these circumstances the presence of the State as a stakeholder often deters managers from hostile behaviour and, although usually the objectives of the State are not clearly identified, one of their main interests, however, may be focused on the provision of public goods (Fox and Heller, 1999) and law enforcement. Following Uhlenbruck and De Castro (1998), however, firms with significant State ownership may promote strategies that are not economically effective and more politically driven. At the same it is recognised that the presence of the State among the stakeholders in privatised former State-owned enterprises (SOEs) is often a big obstacle to restructuring, as State representatives (as new management or board members) are usually non-professionals, and scholars suggest that to achieve effective performance, this non-professional management has to be replaced (Peng *et al.*, 2003).

With the main interest of this research on employee welfare, this literature review will mostly concentrate on managers' and workers' representation, paying less attention to State ownership and non-employee stakeholder concepts.

The "giveaway" voucher privatisation, as a constituent of Russian economic reforms announced in 1992 and implemented to date, boosted employee ownership of enterprises and different governance structures. Privatisations worldwide have been widely studied (see Chapter II) with a focus of its impact on enterprise strategy and performance (Djankov and Murrell, 2002; D'Souza *et al.*, 2001; Megginson and Netter, 2001). Also, studies of employee ownership and control in transition economies have analysed their influence on productivity and financial performance (Blashi and Shleifer, 1996; Earle, 1998; Earle and Estrin, 1996; Frydman *et al.*, 1999). Other researches have focused on the

extent and role of employee ownership in Russia and in some former Soviet Republics (Buck *et al.*, 1994, 1999, 2003; Estrin and Wright, 1999).

The transfer of ownership of the firms to a new legal entity in which managers and workers are significant (if not major) shareholders is usually referred to as a buyout process. The main distinguishing criteria of these buyouts is whether the ownership comes to managers only (managerial buyouts, MBOs), to inside managers and employees (managerial-employee buyouts, MEBOs), or is concentrated in employees' (workers') hands only (employee buyouts, EBOs).

Following common Western experience, managers and workers are those who are likely to take an active part in the governance of the firms because their stakes do not allow them to easily divest their equity in poorly performing firms (Lane *et al.*, 1998). On the other hand, the introduction of significant insider equity stakes is also expected to increase incentives for employees to perform and make decisions intended to maximise firm's profits. In particular, by becoming shareholders, employees could be encouraged to seek involvement in different strategic and operating decisions, like enterprise capitalisation, monitoring themselves, taking part in tasks requiring entrepreneurial judgment on the part of employees, product diversification, etc. More often however, employee ownership and control may encourage employees to act as employees, rather than as effective employee-shareholders, thus choosing wage distribution rather than dividends and capital gains, vast social provisions, lower levels of restructuring and secured jobs (Buck *et al.*, 1994; Wright *et al.*, 1998b). These results also agree with the Fama and Jensen (1983) findings that, for firms with over 50% insider ownership, the question of firm survival takes priority, and employees may insist upon job stability and higher wages rather than be focused on firm's market valuation. From this perspective, employees are relatively risk-averse (Doucouliagos, 1995), which is negative it terms of an influence on performance, but the problem of separation of ownership and control is potentially much less acute in employee-owned firms (Hansmann, 1996).

Workers, therefore, in their dual stakeholder role as employees and as shareholders, are, on balance, likely to choose higher current wages and more social benefits as immediate sources of utility in the short-run, rather than more retained profits, deep restructuring,

long term investment (Buck *et al.*, 1999) and company diversification (Hill and Snell, 1998), resulting in lower profits for Russian EBOs, as they will be dominated by employees. To some extent this is likely to happen because of the expropriation of employees by powerful insiders, such as managers (Filatotchev *et al.*, 2001a). If their views conflict with those of employees, the question who is most salient as a stakeholder, e.g. an owner-manager or an owner-employee, becomes crucial.

From the beginning of the privatisation process, a majority of Russian companies imposed limits on the external sale of shares by insiders. In particular these barriers to "exit" originated with managers (often being legally supported by official privatisation variants too), who discouraged employees' share sales to outsiders. In return, managers assured job security for employees, wages and perquisites, being to some extent paternalistic towards workers and influenced by their needs. Following Filatotchev *et al.* (1999), since employees may prefer current wages to future uncertain wages, they may also be reluctant to sell shares to outsiders, and will sell them to managers, who prefer insider control of enterprises. When managers' stakes increase and reach substantial amounts, they may become entrenched (Morck *et al.*, 1988) and guarantee attractive salaries and employment opportunities for themselves, who, if appointed in the Soviet era, are also concerned about their job stability (not as manager-shareholders) in the face of strong competition from the external managerial labour market.

As a primary conclusion to this *Governance – Strategy* analysis, it is worth noting that most of the theoretical approaches are highly contingent on the environment in which they were developed. The central theoretical problem in governance research is in applying a causal ordering or *a priori* structure to the existing business environment (Peters and Savoie, 1998; Lynn and Hill, 2004). In the face of these challenges and taking into account all theoretical and practical arguments discussed above, this research is of importance in studying the unprecedented privatisation experiment in Russia, where different groups of stakeholders – workers and managers – obtained some control over their enterprises, and were faced with a situation where they had to take decisions on enterprises' strategies which offered immediate welfare – higher wages and social benefits – but probably not enhanced efficiency, higher retained profits, additional investment and restructuring, etc.

Thus, in the context of *Governance – Strategy* relationships, it is possible to hypothesise that:

Hypothesis 1. Higher levels of workers' ownership and closed legal forms will be positively associated with strategies that direct more resources towards immediate sources of employee welfare, e.g. higher wages, job preservation, social benefits, etc.

Of course, such employee-favouring strategies may be expected in a Western context to damage firm performance (to some extent), but here, workers' involvement in corporate governance may offer a comparative performance advantage under certain conditions, e.g., where worker-shareholders may be motivated to practice mutual monitoring on themselves and their colleagues (Earle and Estrin, 1996). Also, in the language of Occupational Psychology, firms' strategies that promote employee welfare may encourage consummate employee contributions to firm performance that are in excess of their contractual obligations (Guest, 1998).

Therefore, following this *Governance – Strategy* review and the introduction of a relevant hypothesis, the next Subsection proceeds to a discussion of *Strategy – Performance* relations, with particular attention to HRM strategies.

3.2.2 STRATEGY – PERFORMANCE

Gaining competitive advantage through different strategic actions has become one of the major focuses of research in the field of strategic HRM in industrialised Western economies (Pfeffer, 1994; Wright and McMahan, 1992; Wright and Snell, 1991). The basis for these researches mostly came from the SM literature, addressing the internal drivers for economic development (Barney, 1991). With the focus of this research on Russian firms, as noted in the Introduction to this Chapter, it is possible to refer to only one *Strategy – Performance* study, by Fey and Björkman (2001), that has examined HRM practices in foreign-owned subsidiaries in Russia. Thus, this research is intended to break

new theoretical and empirical ground by studying the *Strategy – Performance* relationship on a large sample of insider owned indigenous Russian firms. As will be noted later, recent studies by Elenkov (1997, 1998), Holt *et al.* (1994) and Ralston *et al.* (1997) find it important to distinguish Russia and Western firms in terms of theory and strategic practice.

Most Stakeholder Theory, and related strands of the literature of corporate ethics (Bloom, 1999), social responsibility (Harrison and Freeman, 1999; Swanson, 1999) and organisational citizenship (Lambert, 2000), has been more concerned with the general consequences of stakeholder influence on firm performance, as conventionally measured. At the same time, although it was stressed in the contingency theory of SM (see below) that enterprise strategies have to be aligned with a country environment to achieve superior performance, little attention has been paid to the specific case of governance by employee shareholders and their influence on HRM strategies, which could be politically rather than efficiency-driven (Uhlenbruck and De Castro, 1998).

Empirical and conceptual work in the field of HRM suggests that the role of human resources can be crucial to firm performance (Arthur, 1994; Becker and Huselid, 1998; Huselid, 1995; MacDuffie, 1995), but it is also stressed by researches that further studies have to be undertaken. For instance, in the study of the influence of HRM decisions on firm performance, scholars often refer to a need to improve efficiency or contribute to revenue growth.

Since human resources are often viewed more narrowly as a cost needed to be minimised to achieve subsequent gains, reduction in employment is often considered as a main managerial strategy in cutting costs, leading to agency conflict between managers and employees (Charreaux and Desbrieres, 2001). However, the Russian environment represents a form of CG, where a majority of manufacturing firms are employee owned. Even when the ownership appears to be strongly divided between managers and workers, with control concentrated mainly in managers' hands, such decisions as cutting costs through employee dismissals are unlikely to be supported by workers as shareholders, whose shares may help to guarantee their employment (Demsetz, 1983; Fama and Jensen, 1983).

As regards the consequences of HRM strategies for firm performance, Becker and Gerhart (1996) review a literature that studies the impact on firm performance of 27 different measures of HRM strategies in firms from the 1996 Fortune 500 list; Delaney and Huselid (1996) replace conventional performance measures with perceived performance evaluations, based on questionnaire surveys of 590 for-profit and non-profit US organisations from the National Organisation Survey; and Youndt *et al.* (1996) emphasise that strategies addressing employee welfare in 97 manufacturing plants had an impact on performance that interacts with product quality manufacturing strategies. These approaches have, however, so far proved inconclusive in the sense that various HRM strategies are associated with different levels of performance in different circumstances. Nevertheless, these studies do identify unresolved questions for future studies, and their approach to date has not been applied to transition economies.

Berman *et al.* (1999, p.494) employed a sequence of stakeholder relationships → firm strategy → firm financial performance and noted (p.489) "…the potential for HR practices to lower turnover and absenteeism, improve productivity and increase worker commitment and trust". Among other researches undertaken, Youndt *et al.* (1996) analyse the effects of manufacturing strategy on the relationship between HRM and operational performance, as measured by employee productivity, machine efficiency and customer alignment, and find a positive association between them. Becker and Gerhart (1996) conclude that HRM decisions are likely to have an important and unique influence on firm performance. Pfeffer (1994) refers to management "best practices" as elements of high performance, but also identifies that the effect of "best practices" is more likely to be embodied in the structure of an enterprise's system (through motivation, job security, various pay policies, etc.). Delaney and Huselid (1996) find a positive association between a variety of HRM practices and perceptual firm performance measures.

All these scholars argue that organisations can adopt HRM practices that enhance workers' skills and the quality of hired individuals through comprehensive training. The way the workspace is structured affects organisational performance through the degree to which motivated, skilled and trained employees are involved in strategic decisions. Similarly, Osterman (1994) argues that such innovative work practices as teams, quality circles, job rotation and quality management result in productivity and performance gains

as "best practices". However, few of these American practices will fit or have already fitted Russian reality.

According to the contingency approach to strategic HRM, briefly mentioned at the beginning of this Section, the impact of HR practices on firm performance is subject to the firm's overall strategic position (e.g. Schuler and Jackson, 1987). One could argue that developed HR practices are trivial in relation to performance in manufacturing firms, where human capital may be replaced by physical capital, as the central component of manufacturing efficiency. However, Youndt *et al.* (1996) stress that it does not have to be the case, although there are examples of firms competing this way rather than using such modern strategies as cost-cutting or employment flexibility.

According to the behavioural perspective (Schuler and Jackson, 1987; Wright and McMahan, 1992), to achieve effective performance organisational strategies require unique attitudes and role behaviour from employees, and HR activities have to be the primary means of maintaining and intensifying these kinds of employee behaviour. Also, advocates of control theory (e.g. Snell, 1992) highlight the fact that effective performance relies upon correspondence between appropriate HR practices and the administrative environment.

This alignment is essential for the Russian environment, where workers could be very anxious about any cost-cutting strategy that could involve wage cuts or dismissals, and would normally oppose it as major enterprise shareholders. At the same time, workers are likely to favour various HRM strategies, e.g. employee training or investments in intellectual human capital, which will directly increase employees' personal welfare. If employees feel that their voices count and see that managers have an interest in their development, they are more likely to positively respond to managers and produce better outcomes. Subsequently, cost-cutting, improved training quality and other high commitment strategies will be examined in the next Section, as justifying the specific HRM cluster approach in this thesis.

When turning to the managers' perspective within the *Strategy – Performance* analysis, Stakeholder Theory proposes two quite opposite views – the first is that other stakeholders

deter managers from being creative, but the second is that the involvement of other stakeholders may bring about motivational changes that may enhance performance (Driver and Thompson, 2002). Both arguments are usually supported by empirical analyses, including correlations between stakeholding and conditional measures of performance – productivity or innovation (Driver and Thompson, 2002; Lambert, 2000). A prevailing notion in the SM literature is that managers are those who have to cope with a changing environment through a variety of appropriate strategies (Jennings and Seaman, 1994). The leading function of managers is recognised by Kay and Silberston (1995) who argue for a privileged role for managers by giving them (p.95) "...the greatest possible freedom to develop the business over a period of years in whatever way they think fit, while holding them rigorously responsible to all parties involved".

One supporting answer to the question of managerial freedom comes from the history of the steady growth of firms in emerging economies, not heavily dependent on shareholder finance. However, it is worth noting that this growth in emerging economies was often accompanied by violation of stakeholders' rights due to asymmetric information or incomplete contracts – known as the hold-up problem. If the governance of the firms required incomplete contracts to favour certain stakeholders, these contracts would not be feasible (Kay and Silberston, 1995). Hart (1995b, 1996) and Milgrom and Roberts (1992) argue for conferring residual rights to workers, but stress that the hold-up problem will continue to exist if workers get compensation in the form of equity and have a voice over wage determination.

Here, a question of appropriate motivation arises as being crucial for performance in Stakeholder Theory. From this point of view, employee share ownership seems to be a potential answer to the question of employee motivation (Michie and Oughton, 2001). For example, The Companies Act in the UK requires that directors of companies must consider employees' interests in their decision making (Companies Act, 1980). Also the new laws of the European Community allow companies to take into account the interests of stakeholders – creditors, customers, investors and employees (Orts, 1992). However, it has to be remembered that the motivation of employees (as shareholders) in Russia may have been impaired if shares were obtained in the giveaway process without any elements on financial sacrifice on their part (Boycko *et al.*, 1994, 1995).

The detailed content of HRM strategies is important for resulting performance. For example, in terms of different approaches to remuneration forms, variable pay has a low emphasis in Arthur's (1994) "commitment" system, whereas Huselid (1993, 1995) and MacDuffie (1995) emphasise it as a positive influence in terms of Western experience. Abowd (1990) concluded that the degree to which managerial compensation was based on the firm's financial performance was significantly related to future financial performance. Gerhart and Milkovich (1990) found better financial performance in organisations that had remuneration plans contingent on financial results. However, little evidence exists on employee motivation policies and resulting firm performance in transition economies (Uhlenbruck and De Castro, 1998), and particularly in Russian privatised, employee owned manager controlled, companies.

Nonetheless, although exploitation occurred in Russia at many levels after privatisation, in the context of the FSU, paternalism towards workers was generally a consistent feature of enterprise behaviour (*via* provision of social facilities like kindergartens, housing or medical care, summer camps for children, etc.) together with stable employment and substantial training programmes. Following the above discussion it is argued that the most generous firms in Russia in terms of workers' benefits attract the best workers and secure the best performance, in "Soviet" terms at least. It is therefore tentatively hypothesised that this association will continue through economic transition:

Hypothesis 2. Firms' strategies that promote employee welfare will be positively associated with improved corporate performance.

Kaplan and Norton (2001) broaden the focus of managers from traditional financial measures of performance (like return on sales, return on investment, improved profitability, etc.) to a more diverse set, which in particular includes such non-financial measure as organisational learning, in the context of improvements in skills through hours spent on training. Such learning results in higher employee productivity. Following Barney (1991) and Collins and Montgomery (1995), Kaplan and Norton (2001) recognise that HR strategies are path dependent, and could integrate measures that reflect cause-and-effect relations between outcomes (lagged measures), and critical drivers (lead measures) of these outcomes. This concept of multiple-measure systems is generally supported by

accounting theorists, who are focused on revenue growth or future profits, as lag indicators of strategies applied in previous periods. Besides, governance may be expected to have a lagged influence on strategies' relations (Buck *et al.*, 2001). Finally, performance can influence ownership (i.e. governance), either lagged or with simultaneous, reciprocal causation (Wright, 2002; Finkel, 1995).

The decision of lagged effects or cause-and-effect relations depends on the availability of data, and thus reflects whether lagged dependent variables are included as explanatory variables in regression equation (Djankov and Murrell, 2002). In this study we support the view that strategies have an impact on future performance, as most of today's strategies (like training) usually produce outcomes within a number of years, not momentarily. However, as will be noted in the Chapter IV, this research is constrained by using one cross-section of data only (with only a very limited number of parameters measured for two successive years), thus it is not possible systematically to use independent variables for one year and then control dependent variables for the next year, i.e. at least with a one-year lag. This notion represents one of the limitations of this study, addressed in Chapter VI.

Nonetheless, as noted above, Fey and Björkman (2001) examine HRM strategies and performance and find a positive relationship between HRM investments and foreign subsidiary performance in Russia. The authors distinguish "soft" HRM, which has direct employee welfare rather than business performance as its primary concern (Guest, 1998), from "hard" HRM, that leads to improved productivity and better firm performance. This broad distinction between "hard" and "soft" HRM will be developed and operationalised in the context of this thesis, and Section 3.3 starts this discussion.

3.3 HRM Theory and Strategic Clusters

This Section continues a discussion of researches undertaken in the field of Strategic Management and intends to develop an appropriate HRM cluster approach, adopted from the Western literature, for Russian firms in order to be able to propose and analyse

Governance – Strategy – Performance hypotheses in terms of coherent HRM clusters, typical of particular HRM policies. The Section gradually introduces six specific HRM hypotheses, resulting from the above discussion and theoretical views.

Within the last few years a number of researchers have provided anecdotal discussions of HRM issues in Russia, pointing out their importance (e.g. Juplev *et al.*, 1998; Laurence and Vlachoutsicos, 1990; Longenecker and Popovski, 1994; May *et al.*, 1998; Magura, 1998, Puffer, 1997, Radko and Afanasieva, 1999; Shekshnia, 1994, 1998; Welsh *et al.*, 1993). For instance, Longenecker and Popovski (1994) explore managerial trials in organisations in St. Petersburg associated with the transition to a market economy, and conclude that Russian managers have to be retooled with technical and organisational skills to be able to lead their firms. May *et al.* (1998) note specific barriers to the effectiveness of Russian HR managers, observed in specialised group HRM training sessions, organised by US and Russian practitioners in 31 firms across Russia. Shekshnia (1994) examines the "most common myth about Russia" concerning the supposed availability of very cheap and highly skilled workers. This myth causes problems for international investors and undermines the principles of successful investment in Russia. Contrary to the author's 1994 study, the 1998 paper surveys HR management in Russian subsidiaries of Western firms and concludes that Western companies are practicing efficient and sophisticated systems of HR administration and management.

The paucity of Russian HRM research was noted by Fey and Björkman (2001, p.60), who observed that "… little systematic Russian-language research exists on HRM issues and the Western literature investigating Russian management is also very limited".

One major barrier to the replicability of Western research in Russia is that, most Western studies try to establish an empirical relationship between HRM practices and firm financial performance or market value. However, in the case of Russia, the use of stock market-based performance indicators, such as Tobin's *Q*, is fairly inappropriate, as stock markets are thin, firms do not provide tax authorities with accurate data and imperfect disclosure codes make performance indicators rather unreliable too.

Furthermore, in recent studies by Elenkov (1997, 1998), Holt *et al.* (1994) and Ralston *et al.* (1997), a significant difference in the national cultures of Russia and Western countries was noted, and it has been suggested that only specific HRM strategies may be appropriate for Russia (Elenkov, 1998; Fey and Björkman, 2001), which have yet to be tested. Thus, to identify and test appropriate HRM clusters for Russian firms, the Western HRM literature and findings must be modified after reference to specifically Russian research.

HR practices, as individual components of reward systems, affect firm performance not in isolation, but as elements of internally consistent HR "bundles" or system, not individually (Baron *et al.*, 1996; MacDuffie, 1995; Osterman, 1999). The variety of actual HRM practices in different firms must therefore be summarised meaningfully in broad aggregates, although it is not possible or necessary to insist on tight definitions (Osterman, 1999). Moreover, firms have only a limited ability to pick and choose among specific elements of individual policies in structuring employment relations and governance practices, and have to select from among a limited number of HR systems, representing menus, bundles or clusters of HR practices (Baron *et al.*, 1996).

Having once decided to perform *Governance – Strategy – Performance* research with the use of HRM bundles, it is necessary to identify strategic bundles suggested by theory, to develop the required number of distinct bundles, and also to choose specific clusters within each bundle. The term "bundle" refers to the practices that are interrelated and internally consistent, and comprises the effect of multiple practices, combined (clustered) into one specific bundle, thereby reflecting the overall firm's business strategy (MacDuffie, 1995).

The question of identification of bundles of HRM practices confronts most Western HRM research, which includes in particular studies by Baron *et al.* (1996, 1999), Hannan *et al.* (1996), MacDuffie (1995), Osterman (1999, 2000), and Spenner *et al.* (1998). Some of these authors (Baron *et al.*, 1999; MacDuffie, 1995; Osterman, 1999) develop their approach with reference to the *database* of the Stanford Project on Emerging Companies (SPEC), and focus their research on High Performance Work Organisations (HPWOs), as representing a dominant strand in the Western HRM literature. HPWOs originated in the early 1990s and were seen as more productive in terms of output and quality as a result of

a more efficient use of labour, if being compared to the rest of American firms. But, with economic recession, HPWOs were soon faced with a need for restructuring, involving increased layoffs and lower wages, in an environment of organisational turmoil. However, although it was argued that HPWOs would retreat as practices, Osterman (2000, p.183) still claimed that firms performed "...best with substantial employee commitment to the enterprise".

Fortunately, this phase of crisis, with layoffs, global restructuring and widespread recession in the early 1990s is hopefully behind us now, both in Russia, Eastern Europe, and the West. Nevertheless, the great variety of HRM strategies developed within these years of "shock therapy" has to be adopted thoughtfully and with flexibility, accepting the necessity of HRM bundles in empirical research.

However the question of the optimal number of bundles and their appropriate composition is crucial. For instance, Baron *et al.* (1996) and Hannan *et al.* (1996) examine the models of employment relations on a sample of 100 *Bay Area* high technology firms, clustering them into four distinct types – *Commitment*, *Engineering*, *Factory* and *Star Models*. More precisely, the authors refer to the *Factory Model* as "pecuniary attachment, managerial control, hire for current skills"; the *Commitment Model* as entailing reliance on "peer/cultural control, "love" and hire for cultural fit"; the *Star Model* as referring to "attachment to work, professional control, hire for potential"; and the *Engineering Model* as involving "attachment to work (and to a project), peer control, hire for current skills" (Hannan *et al.*, 1996, p.513). In Baron *et al.* (1999), the authors use the described *Commitment*, *Engineering* and *Star Models*, and also introduce *Autocracy* and *Bureaucracy Models*. The latter involves "attachment based upon providing challenging work and/or opportunities for development, selection of individuals based on their qualification for a particular role, and formalised control", while the *Autocracy Model* refers to "employment premised on purely monetary motivations, control through close personal oversight, and selection of employees to perform specific tasks (Baron *et al.*, 1999, p.530). MacDuffie (1995) follows Osterman (1994) in his clustering approach, that distinguishes between practices that affect the organisation of work and the way work tasks are carried out. Delaney and Huselid (1996) separate HRM practices that enhance employee skills from those that motivate employees and those that structure the

workplace. Fey and Björkman (2001) examine foreign subsidiary performance in Russia using three HRM clusters: *Employee Development*, *Feedback Systems* and *Pay/Organisation*, while Ngo *et al.* (1998) identify only two HRM bundles for their Hong Kong study – *Structural Training and Development* and *Retention-oriented Compensation*. Huselid (1995) also uses a two-cluster structure, with one similar to Ngo *et al.*'s (1998) compensation variable – *Compensation and Promotion* – and another concerned with employee feedback and skills development.

Following this wide range of models (in particular within the HPWO literature), "it is not possible, or desirable to insist on tight definitions" of different strategies for Russian research, since "there are important differences in the intensity of work, in health and safety issues, the extent to which gains are shared" (Osterman, 1999, p.100), and there is the embeddedness of employment practices in national culture, founders' philosophy and organisational blueprint dependence in the evolution of employment systems in firms (e.g. Baron *et al.*, 1996).

Nevertheless, some of them implicitly define the three clusters proposed for this research. For instance, the *Star Model* (Baron *et al.*, 1996, 1999; Hannan *et al.*, 1996) applies only to environments where professional organisations impose a strong influence on firms, but the professions have traditionally been weak in the FSU (Filatotchev *et al.*, 2001b); the *Engineering Model* is designed explicitly for the context of high technology Silicon Valley firms. On the other hand, path dependence and organisational inertia are attributed to either an absence of strong competitive pressure (Williamson, 1993) or to patterns of bureaucratisation, administration and managerial intensity that logically follow founders' blueprints of employment relations (Baron *et al.*, 1999). Therefore, institutional inertia and considerable path dependence must be considered as likely features of post-reform Soviet-style strategies in transition economies, and will form the basis for the first HRM bundle in this research, proposed below.

3.3.1 TRADITIONAL SOCIAL WELFARE STRATEGY

This first HRM bundle will be referred here to as the *Traditional Social Welfare (TSW)* strategy, or *Strategic Option 1*. It was noted in the previous Section that "soft" HRM has direct employee welfare rather than business performance as its primary concern (Guest, 1998). This goes deeply into the national culture and traditions of the FSU, where firms were required to make social provisions for employees, regardless of any resulting financial deficit for the firm: deficits that were in any case financed by the State. During the period of transition, some firms continued to provide Soviet-style social facilities for their employees and, as stated above, retained a high level of employment as well, thus attracting State subsidies and acting as a miniature welfare State to some extent. (Of course, some degree of exploitation of the worker also existed.)

Many firms, rather than trying to adopt new strategies under transition, simply followed founders' initial models of the employment relation (Baron, *et al.*, 1999), thus exhibiting institutional inertia. In the Russian case, the founders used a Soviet-style template and those HRM strategies, that mimicked previously-internalised traditional Soviet-style welfare strategies, involving costly resource commitments in the absence of strong competitive pressures, referred here to as the *Traditional Social Welfare (TSW)* bundle. It of course also represents the *status quo*, for Russian firms, and a strategy which, although possibly ill-suited to transition economies to some extent, is familiar to firms and in which they may have established a core competence.

It has to remembered that Russia has generally been identified as having a national culture exhibiting high levels of collectivism (thus low individualism), high levels of uncertainty avoidance and low levels of power-distance tolerance (i.e. a tendency towards egalitarianism) (Elenkov, 1998). This implies a traditional emphasis on values of solidarity, close personal relationships, care for the weak, and protecting past results rather than on taking risks in an uncertain future. In other words this implies that workers are unlikely to support value-maximising restructuring efforts and do not spur performance improvements (Boycko *et al.*, 1996) at the expense of their personal benefits. Employment relationships in the FSU were effectively based on lifetime employment and enterprises

provided many of the social needs of both current and retired employees. The privatisation outcome of managerial and employee ownership may have positive effects on employee motivation and labour productivity (Ben-Ner and Jones, 1995), i.e. insider ownership will be associated with the excessive provision of various social facilities, typical of the "Soviet" model, and described here as the *TSW Strategic Option*. Hence we can hypothesise that:

Hypothesis 3. Higher levels of insider ownership are positively associated with higher levels of Traditional Social Welfare provision for employees.

Following Buck *et al.* (2003), the hypothesised association for *TSW* implies that (p.538) "employee shareholders to some extent will be prepared to sacrifice profits … in the long term for immediate, job-related utility as employees". *TSW* strategy amounts to paternalism by corporations – a form of management practice quite popular in British industrial production in the 19th Century, which has already become a rather unfashionable business strategy in Western firms (Wray, 1996). Following Wray (1996, p.704), "…paternalism exhibits a two-way commitment, with responsibilities and obligations required from both sides" of the employee-manager relationship. Employers do not provide only wages in exchange for work, but are also socially responsible for workforces through benefits and welfare provisions. However, although it still exists in Russia today, *TSW* could survive mostly in an environment offering soft loans from banks or extensive State support (though this has recently become more unusual, with the State attempting to withdraw its ownership and control from the industrial sector), or be feasible within strongly performing enterprises.

It is not surprising that the gradual withdrawal of the State from Russian enterprises has lead to its replacement by other ownership categories – outsiders or private insiders. In the case of private inside ownership, certain legal forms of enterprise (e.g. the open joint stock company) may impose a discipline on senior managers to choose strategies that reduce the threat from outside investors (Buck *et al.*, 2003; Filatotchev *et al.*, 1999). However, Stark (2001) warns that either minor or expected actual changes in property forms may act as a cosmetic device to conceal the *status quo* that in fact is close to the traditional "Soviet" HRM system of welfare provision.

With structural inertia in a *status quo*, any changes to developed routines are harmful *per se*, since they disturb established processes and reduce performance reliability (Hannan and Freeman, 1984). However, changes may have a neutral or positive effect if they are build on existing competences or routines aligned with environmental shifts in the command-administrative economy (Spenner *et al.*, 1998). Thus, in the light of this literature, for the reformed Russian market environment, *TSW* provisions may be expected to be positively associated with enterprise performance.

This positive association may be also supported by the presence of job security (Delery and Doty, 1996; Pfeffer, 1994) in enterprises promoting the *TSW* strategy. Companies that provide their employees with job security signal a long-standing commitment to their workforce, and, as a result, employees are more likely to volunteer productivity improvements. Although the high costs of *TSW* could conceivably damage firm performance in some ways, it was decided to follow Spenner *et al.*, (1998) and hypothesise in this thesis that the *TSW* strategy bundle is expected to be positively associated with the performance of Russian enterprises in overall terms.

To be consistent with *Hypothesis 2* in relation to aggregate HRM strategies and firm performance, it is, somewhat heroically, assumed that the provision of *TSW* benefits in the FSU is uniquely suited to the national culture and institutions of Russia. Specifically, we hypothesise for the *TSW Strategic Option*:

Hypothesis 4. Firm performance is positively associated with Traditional Social Welfare provision for employees.

In other words, we continue to assume that provision of *TSW* benefits in the FSU is uniquely suited to the national culture and institutions in Russia, and thus this specific bundle of *TSW* strategies is positively associated with performance.

Two other important strategies, identified in the Western literature, are quite different to *TSW* and include a *Cost Minimisation (CM)* Strategy (Section 3.3.2) and a *Human Resource Investment (HRI)* Strategy (Section 3.3.3). It has to be remembered, that from the employees' (managers' or workers') point of view, these strategies are not equally

desirable. On the contrary, there are significant differences in the perception of health and safety issues, job security, the intensity of work, and the extent to which gains are shared, benefits provisions and associated costs, etc. (Osterman, 1999). Consequently these strategies could be either opposed or favoured by the employees, and result in stronger or weaker performance.

3.3.2 Cost Minimisation Strategy

The first "hard" HRM strategy, in contrast to "soft" *TSW*, can involve downsizing and "flexible production" (Birkenshaw and Hågström, 2000), characterised by hiring and firing, instead of labour retention. Downsizing, as an HRM policy, has become a popular organisation strategy in the West for improving performance through reducing costs (Luthans and Sommer, 1999), and can also include outsourcing and subcontracting. These business processes are typical of those manufacturing firms in Russia that found themselves in financial crisis after mass privatisation, i.e. in a "business turnaround" situation (Filatotchev *et al.*, 2000), requiring labour retrenchment. In these circumstances, "hard" HRM strategies could be feasible, leading to cost reduction and restoring control over cash flows. This first radical strategy will be referred to as a *Cost Minimisation (CM)* Strategy, or *Strategic Option 2*. It is also identified in the Western literature as "Theory E" (Beer and Nohria, 2000), the *Factory Model* (Baron *et al.*, 1996; Hannan *et al.*, 1996), or *Bureaucracy* or *Autocracy Models* in the studies of Baron *et al.* (1999).

According to Beer and Nohria (2000), in a financial crisis or "business turnaround" situation, drastic changes in strategy (and subsequent cuts in expenditures) may be required. In addition, a company that adopts "Theory E" ignores to a large degree the feelings and attitudes of their employees. As the only legitimate concern of this "hard" approach is shareholder value downsizing, enterprises may lose the commitment, the coordination, the communication, and the creativity from employees, needed for sustained competitive advantage. As shareholders, employees could win under a *CM* strategy, but as employees they are likely to lose, as changes usually involve the heavy use of economic incentives, drastic layoffs, downsizing, and restructuring. Thus, workers' ownership and

control may prevent restructuring, since workers are unlikely to provide any kind of support for layoffs as a starting point for restructuring as a main managerial strategy in cutting costs (Charreaux and Desbrieres, 2001), especially if they still get subsidies (Boycko *et al.*, 1996). The reason for this is that employees may assume that they will personally suffer from retrenchments (Fernandez and Rodrik, 1991, Filatotchev *et al.*, 2000). In the case of the FSU, and following the outcomes of the privatisation programme in Russia (see Buck *et al.* (2003) for Ukraine), increased outside ownership and control and withdrawal of the State, with its system of social provision, have led in many firms to the minimisation of social costs, the implementation of short-term or contractual working schemes with lower wage rates, and other market-related work practices associated with cost minimisation. Thus, it is possible to hypothesise that lower insider ownership and control could be associated with a more active *Cost Minimisation (CM)* Strategy, referred to here as *Strategic Option 2*. Hence:

Hypothesis 5. Lower levels of insider ownership are associated with active Cost Minimisation strategies.

Being a "hard" HRM strategy, "Theory E" is rather common among restructuring US companies, where it is focused on the maximisation of shareholder value and is achieved through financial incentives (Beer and Nohria, 2000). In Russia however, employees may be more concerned with their personal welfare and job stability, rather than the value of enterprise shares, and as a result of a *CM* strategy, may lose any trust in the company and management. Thus it is very unlikely that this strategy will result in improved performance and gains for the firms.

This prediction in relation to the strategy identified here as *Cost Minimisation*, is also supported by the work of Spenner *et al.* (1998), although their work went beyond just HRM strategies, and Buck *et al.* (2003) Ukrainian study. Spenner *et al.* (1998, p.601) argue that drastic, "...core organisational changes will have a negative effect on organisational performance". On this view, any governance changes that radically depart from the old practices (in the case of Russia, the Soviet command-administrative economy) and, on the contrary, implement unrestrained market practices, would be extremely damaging for the performance outcomes of the firms (Ernst *et al.*, 1996), in the

early years at least. Therefore, following Buck *et al.* (2003), Ernst *et al.* (1996) and Spenner *et al.* (1998) it is assumed that cost-cutting in relation to employment costs runs contrary to the national culture, philosophy and institutions of Russia, and is unlikely to result in improved performance. Hence we hypothesise that:

Hypothesis 6. Firm performance is negatively associated with Cost Minimisation strategies.

Under the influence of private inside owners, a number of the State's HR practices were transferred to the firms themselves, and thus replaced the old system with a new one, based on low-commitment, high-turnover employment relations (MacDuffie, 1995; Osterman 1999, 2000). This type of firm, also denoted as being based on the *Factory Model* (Baron *et al.*, 1996; Hannan *et al.*, 1996), is characterised by pecuniary attachments, hierarchical managerial control and hiring for current skills. Following Baron *et al.* (1996), the *Factory Model* is based on purely monetary motivations, control and coordination through formal managerial control and selection of employees to do predetermined tasks (with no or very limited training provided). The similarity between a workspace as a "factory" and a traditional industrial factory of early capitalism comes here from the notion that employees are considered as technical inputs with tight bureaucratic control. Unsurprisingly, firms using the *Factory Model* may employ a minimalist (*CM*) HRM strategy compared with those using a *TSW* (above) or *HRI* strategy, discussed in the next Section.

Following the above discussion, a *Cost Minimisation* strategy is considered as departing most decisively from the antecedent Soviet founder's employment model, and is hypothesised as being damaging in terms of performance outcomes for Russian firms (in the short term at least), and resulting from decreasing insider shareholdings and control.

3.3.3 HUMAN RESOURCE INVESTMENT STRATEGY

In stark contrast with *Cost Minimisation*, Beer and Nohria (2000) develop the HPWO literature, and refer to "Theory O", involving long-term, high commitment investments in employees with the purpose of raising performance and productivity, in an attempt to establish a "psychological contract" between workers and their firms. "Theory O" also calls for radical departure from traditional Soviet HRM practices, although less drastic than "Theory E", and is identified in the Occupational Psychology literature with "psychological contracts", where employees are provided with informal guarantees concerning employment stability and insurance provisions in exchange for their commitment to the enterprises (pay as fair exchange). This HRM strategy will be referred to as a *Human Resource Investment (HRI)* Strategy or *Strategic Option 3* in this research.

It is worth noting that following "Theory O", *HRI* is a "hard" HRM alternative to the "flexible" firm and labour retrenchment, but an HRM strategy that involves investments in employees (both retained and newly hired). The goal of "Theory O" is to develop a corporate culture and human capability through individual and organisational learning (Beer and Nohria, 2000) to achieve superior performance. Following Vlachoutsicos and Lawrence (1996), investing heavily in managerial learning of Russian partners and employees was observed as a common feature of successful joint ventures.

This third, high-commitment, Western HR model also corresponds to that identified by Osterman (1999, 2000), who examines HPWO practices in relation to productivity and quality gains that are to some extent shared to employees' benefit. (His low commitment model comprises features associated here with the *CM* model.) The conventional view has always been that in order to achieve high commitment from the employees, firms also have to make a reciprocal commitment (Osterman, 1999) or contribute to "psychological contracts" (Dore, 1992; Guest, 1999) so that "flexible" employees would not require extensive vertical monitoring and high buffers stocks. "Flexible" or "lean" production is also identified by MacDuffie (1995) and Baron *et al.* (1996) with a high-commitment HR strategy, which requires motivated, skilled and adaptive workers that in combination with reduced stocks could create the conditions under which innovative HR practices are most

likely to yield effective economic performance. On this view, employees who have strong emotional ties to their firm and feel that their opinions count, are those who believe that their managers are interested in their development (i.e. emotional/psychological engagement), and are more likely to produce favourable outcomes and thus improve firm performance (Luthans and Peterson, 2002).

High-commitment "psychological contracts" that lead employees to contribute efforts on behalf of the firm that exceed any contractual obligations (Guest, 1998), can theoretically result in strong efficiency gains for the enterprise (Barberis *et al.*, 1996), and in the development of human resources, through different forms of training and education. It is known that technological skills were on a high level in the FSU due to good education in natural sciences, especially engineering and mathematics. But when Russian enterprises found themselves in a market environment, where they now have different tasks, and individuals are required to develop other skills (often based on tacit know-how), the provision of various forms of training and developmental investments for employees (including team-based performance compensation programs) became essential. Russian organisations can also improve their HRM by giving team-based financial awards on a monthly, quarterly, and annual basis for achieving a variety of targets. So, it can be hypothesised that:

Hypothesis 7. Higher levels of insider ownership are positively associated with the intensity of high-commitment Human Resource Investments.

Subsequently, following Fey and Björkman (2001), who empirically proved that *HRI* strategies in foreign subsidiaries in Russia are positively associated with improved firm performance, and Buck *et al.* (2003), who have drawn a similar conclusion for high-commitment HR strategies in Ukraine, we can hypothesise that:

Hypothesis 8. Firm performance is positively associated with new HRI investments.

One may argue that a similar *HRI* strategy could be pursued by foreign entrants too. However with the main focus of this research on insider owned Russian firms, we do not consider the examination of outsiders in this thesis.

The *HRI* model is proposed here as one involving high commitments from both the firm and employees, involving team-based (rather than individual) compensation, where the latter is more typical of the *TSW* model. However, it is clear that the *HRI* model has more in common with the fundamental philosophy of the *TSW* model than *CM*, and is directly concerned with employees' welfare, as a primary source of sustaining competitive advantage for a firm (Pfeffer, 1994). To this extent, *HRI* implies a less radical departure from *TSW* than *CM*.

Therefore, following MacDuffie (1995) and Spenner *et al.* (1998), the *HRI* strategy is another variant of the high commitment model that departs from direct financial and in-kind subsidies to employees, and represents investment in an enterprise's human resources and the introduction of new – performance-related – incentive schemes, aligning them with environmental shifts, e.g. those that have occurred during transition.

As stated, the *HRI* strategy is proposed here as involving commitments to initial and ongoing training as well as team-based compensation, rather than the individual contingent contracts associated with the *TSW* and *CM* models. Also, the *HRI* strategy can be viewed as a "total quality" strategy that focuses on continually improving manufacturing performance via investment in human capital (Garvin, 1993). More specifically, employees in such environments are required to make the transition from a labour force providing only physical work effort, to empowered intellectual capital whose responsibilities expand to include such activities as planning, problem solving, quality assurance, etc. (Snell and Dean, 1994, 1995; Youndt *et al.*, 1996). This requires a skilled and motivated workforce that has the knowledge and capability to perform the required tasks (Pfeffer and Veiga, 1999). Since employee development can be expected to be an important determinant of enterprise performance in Russia, a variety of *HRI* practices is related to the development of the human resources of the firm itself. Thus for instance, enterprise investments in technical and non-technical training are likely to be positively associated with the "...extent to which the company actually succeeds in developing the skills and knowledge of its employees" (Fey and Björkman, 2001, p.62). The positive relationship between employee training, as one of the high commitment HRM practices, and firm performance was also found by Delaney and Huselid (1996), Huselid (1995),

Koch and McGrath (1996), and MacDuffie (1995). Besides raising productivity, however, training clearly involves costs too.

Following the preceding discussion, the *HRI* strategy is expected to work best in an environment where employees are willing to learn new skills and improve their quality and productivity. The HRM literature provides a conventional view that employees are willing to make this kind of commitment (Osterman, 2000). In a survey of private sector non-managerial workers and low- and mid-level managers, Freeman and Rogers (1995, p.340) find that "...some 79% of non-managerial participants in employee involvement programs reported to personally" benefit from participation "...by getting more influence on how their job is done". To large extent this perception was achieved due to performance-based compensation as a prominent feature of high-involvement HRM practices. This has also been reported in other Western studies (e.g. Arthur, 1994; Delery and Doty, 1996; Delaney and Huselid, 1996; Huselid, 1995). Following Fey and Björkman (2001, p.64), these authors "...have identified performance-based compensation as the single strongest predictor of firm performance". However, until recently very few local Russian companies were making use of pay in this way to reward employees (May *et al.*, 1998), although this practice was quite common and successful in the Russian subsidiaries of Western firms (Fey *et al.*, 1999; Juplev *et al.*, 1998; Puffer, 1997; Puffer and Shekshnia, 1994). Being recognised as a prominent characteristic of *HRI* strategies in Western research, team-based performance pay is included here in the *HRI* strategic cluster, as opposed to the individually-oriented bonuses, typical of *CM* strategy.

According to the above discussion, an *HRI* strategy is considered as a "hard" strategy departing least from the antecedent Soviet founder's employment model, and was hypothesised as being positively associated with the performance outcomes in Russian firms and supported by firm insiders.

3.3.4 MIXED HRM STRATEGIES AND SUMMARY ON APPROPRIATE BUNDLES FOR RUSSIAN RESEARCH

The preceding Section identified three strategic HRM bundles (with corresponding hypotheses introduced), recognised in Western research, for the analysis of *Governance – Strategy – Performance* relationships in Russia. Specifically, these bundles comprise *Traditional Social Welfare (TSW)*, *Cost Minimisation (CM)* and *Human Resource Investment (HRI)*. The analysis shows that, although the *TSW* and *HRI* strategic bundles are quite distinct in terms of their underlying factors, they both represent high commitment models. From this perspective, the proposed *HRI* model is argued to be a gradual departure from traditional HRM in the FSU. The *CM* "hard" HRM strategy departs from the traditional Soviet HRM model most decisively.

Meanwhile, the question arises, what if a company chooses a sequence of strategies or decides to apply them simultaneously, mixing, for instance, *CM* with *HRI*? According to Beer and Nohria (2000), companies can enact "Theory E" (*CM*) and "Theory O" (*HRI*) in sequence. For example, a company can first layoff employees ("Theory E") and then cut down organisational hierarchy and start investing into training of remaining employees' ("Theory O"). Additionally, if *HRI* follows *CM* strategy, employees and managers may feel betrayed, and, normally, it is too hard to manage these circumstances (Beer and Nohria, 2000).

Also following Beer and Nohria (2000), instead of using only one strategy or their sequence, a company could try to implement both *HRI* and *CM* at the same time. The authors argue that in this case the simultaneous use of both HRM strategies is more likely to be the source of sustainable competitive advantage, although it has to be remembered and understood that the goals of these two policies explicitly conflict.

Lepak and Snell (1999) also noted that firms can utilise multiple HRM strategies, especially if these are "make/buy strategies", which are not mutually exclusive. However, Sonnenfeld and Peiperl (1988, p.597) maintained that "...each firm should exhibit one

modal type of the system, which we would expect to be most closely connected with the base, or primary, business strategy", a position that the empirical literature in the strategic HRM field generally supports (Bae and Lawler, 2000).

Following this discussion, it becomes clear that the process of mixing or sequencing two HRM strategies becomes a balancing act between initiating actions that follow one strategy and then deviating from that strategy. It also takes years and highly skilled management to fully implement one strategy, and if, during the process, senior management is changed, the program may lose momentum and direction. To estimate HRM strategies applied in sequence or in mix, one would require a time series of data, however. With the real possibility that Russian managers may not be qualified to promote commercially-oriented strategies, and due to the constraints imposed in this thesis by only one cross-section of data, we therefore leave this issue as being beyond the bounds of this study.

Meanwhile, the question arises, how significant may these three broad strategies be for Russian firms? In existing research, Longenecker and Popovski (1994), May *et al.* (1998), Puffer (1993), Radko and Afanasieva (1999), Welsh *et al.* (1993) have suggested that modern HRM policies are crucial to success in Russia. Fey and Björkman (2001) investigated the relationship between HRM and firm performance in 101 foreign-owned subsidiaries in Russia and found that greater HRM investments for managerial and non-managerial employees are positively related to firm performance, e.g. labour productivity improves. This finding coincides with a resource-based view of the firm and provides support for the investments in high-commitment HRM strategies that aim at getting more from workers by giving more to them (Baron and Kreps, 1999).

The following table summarises the range of models and methodologies, used in Western or CEE (Spenner *et al.*, 1998) studies, which were found to closely correspond with the three coherent clusters proposed for this Russian research – *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment*, and thus supporting their choice.

Table 3. Some of the Recognised Models and Methodologies Used by Authors

Authors and Methodologies [1]	*Traditional Social Welfare* Equivalents (plus Associated Concepts)	*Cost Minimisation* Equivalents (plus Associated Concepts)	*Human Resource Investment* Equivalents (plus Associated Concepts)	Additional Models
Baron *et al.* (1996) 100 *Bay Area* hi-tech firms, Cross-section plus Weighted Least Squares	Founders' Organisational Models	*Factory Model* (Cost Minimisation)	*Commitment Model* (Lean Production)	*Star* and *Engineering Models* [2]
Baron *et al.* (1999) SPEC, Cross-section plus Weighted Least Squares	Founders' Organisational Models	*Bureaucracy* or *Autocracy Models* (High Managerial Intensity)	*Commitment Model* (Lean Production)	*Star* and *Engineering Models* [2]
Hannan *et al.* (1996) SPEC, Cross-section	Founders' Organisational Models	*Factory Model* (Cost Minimisation)	*Commitment Model*	*Star* and *Engineering Models* [2]
MacDuffie (1995) Cross-section plus Factor Analysis, Reliability, Cluster Analysis	Only concerned with HRM innovations	Mass Production (Low Commitment, Taylorism)	High Commitment (Flexibility, Empowerment)	Transitional Model, Low to High Commitment
Osterman (1999, 2000) Two Cross-sections, Descriptive Analysis, OLS	Only concerned with HRM innovations	Low Commitment	High Commitment (High Performance Work Practices)	
Spenner *et al.* (1998) Bulgarian Panel, OLS	Command-Administrative Economy	Core HRM Changes	Peripheral, Incremental HRM Changes	

[1] Methodologies will be examined in full detail in Chapter IV.

[2] The *Star Model* is only relevant to an environment where professional organisations impose strong controls. The *Engineering Model* is described by Hannan *et al.* (1996) as the Silicon Valley Model, and is concerned with project attachment and peer control.

As can be seen from the table, Baron *et al.* (1996, 1999) and Hannan *et al.* (1996) refer to a founders' model, which embeds employment practices, institutions and national culture, and follows the founders' philosophy and organisational blueprint in the evolution of firm employment system. In the case of the FSU, the concept of *Traditional Social Welfare* corresponds with a founders' model. Although it could be very costly to implement in the post-reform transition environment, *TSW* must be considered as an important "soft" HRM strategy that has direct employee welfare rather than business performance as its primary concern (Guest, 1998), and thus is expected to be adopted in employee-controlled enterprises. In other words, a Stakeholder perspective can be combined with HRM bundles to generate predictions in relation to strategies. Furthermore, *TSW* strategies, associated with employee ownership, may be associated with inferior firm performance.

The *Factory*, *Bureaucracy* and *Autocracy Models*, used by the same authors, together with strategies denoted elsewhere in the Western literature as mass production, Taylorism or low commitment (MacDuffie, 1995; Osterman, 1999, 2000), represent a family of models corresponding to the *Cost Minimisation* strategic option. This "hard" HRM strategy is focused on improving effectiveness through reducing costs via massive layoffs, downsizing, and "flexible production" (Birkenshaw and Hagström, 2000), etc. This model is characterised by high-turnover labour relations (where employees are hired for short periods to perform particular tasks), low-commitment from both sides, as employees lose any trust towards the company and its management. This *Cost Minimisation* strategy deviates most decisively from the founder's model of employment in the FSU.

Again, links between governance through stakeholders and HRM strategies and hence performance may be proposed. Where enterprise employees represent a majority of inside owners, it is argued that the *CM* strategy will be seen to be damaging and will therefore be opposed by insiders, since it brings job instability to employees and cuts in social provisions. In the context of the FSU, it is also argued that *CM* is negatively associated with firm performance.

The *Human Resource Investment* model is recognised by Baron *et al.* (1996, 1999), Hannan *et al.* (1996), MacDuffie (1995), Osterman (1999, 2000), and Spenner *et al.* (1998) as a high commitment HRM strategy, built as a development of the *TSW* model. In

particular, it involves long-term investments in employees (e.g. training) with the purpose of raising productivity and performance in an attempt to establish a "psychological contract" between workers and firm, where workers are provided with informal guarantees concerning employment stability and benefits. Employee-shareholders may be expected to be associated with such strategies and although, being a "hard" HRM strategy, it is less radical than the *CM* strategy, and is more likely to produce favourable outcomes and improve firm performance (Luthans and Peterson, 2002).

To summarise, in order to extend previous studies of HRM practices in the West and in the FSU, and Russia in particular, this analysis adopts three coherent HRM bundles, the first based on institutional inertia – *TSW*, the second founded on radical economic change – *CM*, and the third involving a development of high-commitment founders' blueprint – *HRI*.

3.4 CONCLUSION

To conclude this Chapter, it seems clear that important gaps in the literature have been identified in relation to (a) the influences of governance (besides MBOs and takeover) on HRM strategies and (b) the consequences of these HRM strategies for firm performance in transition economies. Finally, (c) there has been no analysis of the inter-relations between governance, strategies and performance. In this sense, this research breaks new ground theoretically and empirically by studying employee welfare strategies in the FSU, specifically Russia.

As globalisation continues and it becomes clear that human resources are the real competitive advantage, effective HRM becomes crucial for enterprise performance. The challenge facing international HRM is not whether to use recognised and already adopted concepts, frameworks and techniques, but rather how to effectively adapt and fit them across cultures (Luthans *et al.*, 1997). There is also a growing debate on which HRM model to adopt – "soft" or "hard" for successful *Governance – Strategy – Performance* relations. The literature review in this Chapter would suggest that most of the countries

that went through transition firstly demolished the old system of employment relations, and then started building new cost-effective strategies – either *Cost Minimisation* or *Human Resource Investment* strategies. In most of the countries studied, after years of economic distress, the situation was generally improving and enterprise owners started investing into employees.

The insider ownership generated by the Russian mass privatisation programme, encourages the firms to treat employees as assets and source of competitive advantage. Subsequent chapters are intended to give answers to the question of whether the stakeholder rights of employees influence strategic decisions in favour of immediate sources of their welfare (employment, high wages, social benefits, etc.), and how this impacts on performance. In terms of a cluster approach, developed in the review of relevant HRM literature, above, available data will be exploited to see if the adoption of the three broad strategies (*Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment*) can be also attributed to the extent of insider ownership. In addition, once the *Governance – Strategy – Performance* relations are considered as interdependent, the chosen methodology, therefore, will accommodate interactions between governance, HRM strategy and performance. This methodology is described later in the next Chapter.

CHAPTER IV. Data and Methodology

4.1 INTRODUCTION

Most of the literature on Corporate Governance and Strategic Management, that provided research basis for this study in Chapter III, led to quantitative analysis. There is a prevailing view that quantitative variables are to be trusted more, even with the misreporting and accounting difficulties that are rife in transition countries (Djankov and Murrell, 2002). Nonetheless, quantitative variables can measure directly the output of enterprise restructuring and economic performance. There is also the view that "quantitative performance might suffer when an enterprise is investing in large-scale reorganisation and that the results of this process might be observed earliest in qualitative variables" (Djankov and Murrell, 2002, p.750).

However, although the techniques for conducting and reporting qualitative research are fairly similar to quantitative ones, the nature of qualitative study (based mostly on the collection of case study information) has led to distinguished articles on the topic (Moore *et al.*, 1986). According to Van Maanen (1983), the label "qualitative methods" has no precise meaning in any of the social sciences. The author states (p.9) that "it is at best the umbrella term covering an array of interpretive techniques which seek to describe, decode, translate, and otherwise come to terms with the meaning, not the frequency, of certain more or less naturally occurring phenomena in the social world". Qualitative research seeks to describe and explain particular phenomena which under investigation (Marshall and Rossman, 1989). Questions and problems in qualitative research are usually derived from real world observations, dilemmas or questions, and take the form of wide-ranging inquiries (Marshall and Rossman, 1989) that produce descriptive data from persons' written or spoken words (Bogdan and Taylor, 1975). In other words, a study that attempts to uncover the nature of people's experiences as a social phenomenon naturally lends itself to qualitative types of research (Strauss and Corbin, 1990).

Some researchers are concerned about reliability and validity in qualitative research (Delamont, 1992; Goetz and LeCompte, 1982; Lincoln and Guba, 1985; Merriam, 1988). Most theorists agree that concerns of reliability and validity can be addressed in qualitative research, albeit from a different perspective than in quantitative studies (Delamont, 1992; Lincoln and Guba, 1985; Merriam, 1988). These researchers argue that since qualitative research is based on people's experiences and assumptions about reality, it should have different conceptualisations of validity and reliability (Merriam, 1988), and should be applied to case studies mostly.

With a rich basis for research coming from the questionnaire data collected, this thesis favours the quantitative approach and is developed in the manner where hypothesised relationships between various strategic and governance factors are tested using methods of statistical analysis in order to accept or reject possible associations with certain levels of significance.

This Chapter starts with Section 4.2 on Survey Methodology and Data Collection, turning next to Sample Representativeness and sampling issues. This Section is concerned with empirical data collection and the choice of data collection methods adopted in the conduct of this research. It also explains the main stages of questionnaire design, and provides a theoretical discussion and sample comparison with official Russian statistics. With the focus of this thesis on a wide range of HRM practices adopted for Russian privatised firms, Section 4.3 continues with an in-depth description of the Questionnaire Design, paying particular attention to question types, scales and other topic-related sections included into the questionnaire for obtaining relevant information and measures during the survey process. Then, on the basis of described questionnaire, Subsections 4.3.1, 4.3.2, and 4.3.4 introduce correspondingly Main Independent Variables, Main Dependent Variables and Controls for *Governance – Strategy* and *Strategy – Performance* analyses. Also, Subsection 4.3.3 describes Composite Strategic Variables for the specified cluster analysis applied in this research. Subsections 4.3.1 – 4.3.4 also discuss the relevance of introduced measures for testing of the stated hypotheses. Where needed, descriptive analysis backs up the choice of selected measures.

Next, Section 4.4 provides a fundamental description of Statistical Techniques with a particular focus on:

- 4.4.1 Statistical Assumptions for Econometric Models;
- 4.4.2 Examination of Regression Parameters;
- 4.4.3 Modifications of Regression Models; and
- 4.4.4 Cluster Analysis.

Subsequently, Section 4.5 provides theoretical grounds for the specified cross-sectional study, as opposed to time series analysis, paying attention to the strengths of cross-sectional approach, as well as addressing its associated weaknesses.

Section 4.6 hereafter presents Models and Specifications, which will be tested in support of the hypothesised relationships between *Governance* and *Strategy* (4.6.1) and *Strategy – Performance* (4.6.2). Subsection 4.6.3 describes Composite Strategy Models proposed here for adopted *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* specific HRM bundles' approach.

The Chapter is concluded with Section 4.7, which provides a summary on data; methodological background; statistical techniques; models, variables and controls used in this thesis.

4.2 Survey Methodology: Data Collection and Sample Representativeness

During the years of transition, Russia has not generally been a subject of intensive research, being considered by the West as descendant of the Soviet economy of central planning and tight norms, arguably declining, unstable, unreliable, etc., and only years later as a growing economy in the middle of a world recession, that has attracted interest from researchers. As was noted by Fey and Björkman (2001), little systematic Russian-language research existed on HRM issues in Russia, and the Western literature was very limited too. Thus, with regards to empirical data collection this thesis followed many of

the approaches of previous studies in transition economies. This is particularly the case with HRM strategies where employee ownership and control remains high by Western standards.

This research is based on unpublished surveys collected in Russia during the year 2000 (with some 1999 comparisons) by the International Labour Organisation (ILO) in Geneva, Switzerland, as part of its traditional Russian Labor Force Survey. The author had no opportunity to influence questionnaire development and the survey process, which used two questionnaires and was thoroughly performed by ILO professionals.

Regarding the survey instrument, both questionnaires were developed in English and then translated into Russian. The first questionnaire was piloted by mail (with a return envelope) with general directors of enterprises in Moscow, the Moscow region, St. Petersburg, Nizhni Novgorod, Ivanovo, Vladimir, Chelyabinsk and in the Republic of Tatarstan. The second questionnaire was administered through face-to-face interviews with general directors or senior managers of enterprises in the same regions. Both of the results were revised and back-translated into English afterwards (Standing and Zsoldos, 2000).

There are a number of responsiveness issues related to the use of both of the described methods of data collection. One of the major problems regarding the questionnaire-based interviews in Russia is a low response rate, caused mostly because of unfamiliar methodology (especially for indigenous Russian firms), and, also, the time-taking nature of the process. Following Filatotchev *et al.* (2001a), Russian managers were often reluctant to spare their time when being invited to participate in a number of surveys, conducted by Western researchers and professionals. Here, one of the ways to overcome the spare time issue was to conduct a face-to-face interview, whereas, the first obstacle could be escaped by simple wording and terminology of questionnaire. Thus, this was one of the reasons to use questionnaires translated into Russian, and conduct face-to-face interviews during the second stage of data collection process. The presence of ILO professional agents at State Committee of The Russian Federation on Statistics (Goskomstat) was considered necessary to secure accurate completion of a long, complicated survey instrument.

Following Standing and Zsoldos (2000), over the last eight years ILO has conducted a number of Labor Force questionnaire Surveys in developing and transition economies, like Azerbaijan, China, Indonesia, Malaysia, Moldova and Ukraine. For each of these countries questionnaire design has been modified and individual parameters, measure and scales were introduced to match survey environments and local conditions of these countries, particularly country-specific HRM practices (Standing and Zsoldos, 2000). For Russia, these in particular included such important HRM variables as a number of laid-off workers, benefits paid in-kind, plans to reduce social provisions, etc.

ILO gathered objective and perceptual data on HRM practices and perceptual indicators of organizational performance from 309 enterprises. However, direct quantitative information on firms' financial performance (like firms' value, profitability or other accounting based information) was not collected. For some measures, like organizational size or a number of lay-offs, respondents provided extensive factual data. The obtained sample contained numerous information on enterprises with different property forms: State-owned enterprises, producer co-operatives and partnerships, closed and open joint stock companies (JSCs), and private firms. A number of questions in the 2000 survey were designed and answered for the year 2000 and also for 1999. These are for example: a percentage of sales exported within or outside the CIS, or bartered; a total number of workers and employment change (resigned/dismissed); paying for special training institute; social costs', training and wage share of production costs. Also, the survey contains data on such governance variables as share ownership of different groups (where insider ownership is of our particular interest), legal forms of enterprises, and other elements like profit sharing system, etc.

A final sample (referred to hereafter as the ILO sample) was obtained from 295 firms giving useable responses from Moscow, Moscow Region, Nizhni Novgorod and Ivanovo by means of reduction of the original ILO sample according to missing values. This sample reduction did not change the total sample industrial distribution significantly as these two samples are generally within 0.02% of each other. Following Standing and Zsoldos (2000), enterprises themselves were systematically selected using a random start with probability rates based on population proportions according to employment size, i.e.

with a 50% probability rate of being selected for "large" enterprises, 25% for "medium-size" firms and 25% for "small" ones.

This approach is similar to the one for Ukrainian ILO questionnaire survey, where The Ukrainian Ministry of Statistics required regional State statistics departments to collect data from a particular number of enterprises, based on the sampling procedure described above. From this point, Ukrainian questionnaires resemble more an official census than an academic survey once the returns were compulsory, and "the accuracy of quantitative data was checked by surveyors against what is called the official "balance sheet" of Ukrainian establishments" (Buck *et al.*, 2003, p.539). Although The Russian State Committee on Statistics did not enforce any participation conditions, as its Ukrainian counterpart did, similar selection process implies quite high reliability rates of data for Russia too.

In this context, it should be emphasised that the author had no control whatsoever over the survey process, and the only discretion involved his extraction of relevant responses and the construction of clustered variables from a large number of questions. While this situation obviously involves risks in terms of validity and non-response bias, etc., the upside is that ILO professionals gained access to Russian firms, producing a massive survey that would have been quite beyond the resources of a single PhD research student. Some tests on representativeness can be used, however.

The final sample of 295 enterprises (with 95% of independent firms, and the rest 5% constituting part of bigger establishments) covers 184,874 employees from Metallurgy, Engineering, Food and Light industries, Chemistry, Wood & Paper, and Construction materials (Table 5 beneath). The majority of responded general directors were male – 260 (or 88%) – and the rest 35 (or 12%) were female. Directors also averaged 14.3 years at their enterprise and 7.6 years in their current position. Table 4 presents sample property form and detailed employment distribution:

Table 4. Property Form Distribution and Employment Percentages

Property Form	Number of Enterprises	Number of Enterprises (%)	Number of Employees	Employment (%)
State	45	15.25	24,394	13.19
Partnership	37	12.54	16,536	8.94
Closed JSC	64	21.69	35,185	19.03
Open JSC	149	50.51	108,759	58.83
Total	295	100	184,874	100

It can be seen from the table that State enterprises accounted for only 13.19% of people employed, while open and closed JSCs had 58.83% and 19.03% respectively. Similar proportions come for the number of enterprises in each of these groups. The Table also shows that among 295 enterprises included into the sample, State enterprises embrace only 15.25% of the sample, and open and closed JSCs represent 50.51% and 21.69% respectively. Partnership was found to be the least popular governance form in the ILO sample, both in terms of the number of enterprises presented and people employed.

The choice of sample appears to be one of the most primary concerns of survey studies (Mouly, 1978). For example, collected data for a number of regions may not be representative of the population of the country. However, sampling methodology also depends on the subject of interest and general scale of research (Moser and Kalton, 1971). It has to be remembered that the ILO survey was not intended to be representative of the country as a whole, nor for all industrial sectors. In fact, it was restricted to manufacturing enterprises in the major regions listed above. In support of this (but remembering that our sample covers only 295 firms in the selected regions), in Table 5 we provide industrial distribution of the ILO sample, together with it's comparison with the official population of Russian firms in terms of employment in the selected regions.

A potential selection bias in the surveyed sample may be expected due to the possibility of non-response, which represents one of the serious limitations for all survey-based analyses. However, representativeness improves when comparing ILO results with the

official Russian statistics on employment figures in Moscow, the Moscow Region, Nizhni Novgorod and Ivanovo. It is known that the former Soviet system gave high priority to "material production" and to the military-industrial orientation of enterprises, so it is of no surprise that Engineering represents the largest group in both official Russian statistics and in the ILO sample. With engineering having a half of the sample, the second largest industry is the Light industry with approximately 22% among the surveys enterprises. Also, close correspondence can be seen between Food, Chemistry, Wood & Paper, and Industry of Construction Materials. The least represented industry within these four regions is Metallurgy, which is covered by only 3 enterprises in the ILO sample, but does not vary a lot from this in terms of people employed within official Russian statistics too.

Table 5. Industrial Sector Classification of the Sample and Comparison with Official Russian Statistics

Branch of Industry	ILO Sample			Official Statistics [1]
	Number of Enterprises	Number of Employees	Employment, (%)	Employment, (%)
Metallurgy	3	1,186	0.64	0.51
Engineering	109	92,705	50.14	48.36
Food	45	12,694	6.87	7.24
Light	72	40,548	21.93	22.21
Chemistry	18	26,402	14.28	13.6
Wood & Paper	27	4,749	2.57	4.37
Construction Materials	21	6,590	3.56	3.71
Total	295	184,874	100	100

Data source: [1] Russian Statistical Yearbook 2000 (State Committee of The Russian Federation on Statistics, Moscow, 2001)

The use of the ILO data overcame many of the difficulties highlighted in previous studies on the FSU and Russia, e.g. by Blasi *et al.* (1997); Buck *et al.* (1999); Earle (1998); or Estrin and Rosevear (1999), who pointed out the lack of available and reliable data for research. On the contrary, the ILO sample provided a broad array of information on a representative sample of Russian firms.

The original ILO questionnaire consisted of more than a hundred major questions. It was already noted, that the author had no control over the design of questions or their administration, though both were subject to a high degree of professionalism within the ILO and Goskomstat professionals (in some regions, local Goskomstat employees were recruited by the ILO to handle the survey process). With the focus of this research on *Governance – Strategy* and subsequently *Strategy – Performance* mechanisms in relation to HRM strategies and employee welfare, we use only relevant measures that can be applied as testable components of the hypothesised relationships. Appendix I embraces the selected variables and forty-one relevant questions in full detail. The next Section (with a number of subsections) provides theoretical grounds for the choice of independent variables, dependent variables, composite strategic variables, and controls.

4.3 Questionnaire Design and Measures

It was noted at the beginning of Section 4.2 that the ILO survey was conducted through two questionnaires: the first piloted by mail with general directors of enterprises, and the second administered through face-to-face interviews with general directors or senior managers. This survey process benefited from the use of extensive ILO professional knowledge of Russian post-privatisation restructuring processes and industry organisation.

The survey was conducted through the personal distribution of questionnaires and in both stages, general directors were made aware of the survey personally or via phone in advance, to reduce the possibility of non-responses. The first questionnaire was piloted in the middle of 2000, and the second stage of face-to-face interviews took place by the end of that year. The majority of questions were designed to be answered for the year 2000,

sometimes backed up by the 1999 comparisons (i.e. for the period of July 1999 – July 2000). Some additional information was obtained during the interviews, but primarily, due to its qualitative nature, it was not included into the data.

The questionnaire consists of: (1) open-ended questions, where respondents were asked to provide either precise numerical values (like enterprise size, turnover rate or amount of earnings), or percentage data (e.g. on shares held by insiders or outsiders); (2) general "yes", "no" or "do not know" questions regarding any strategies or practices taking place; (3) multiple choice questions (existing types of remuneration system or a list of benefits provided); and (4) a number of classification questions (region, industry, property type, etc.).

The questionnaire opens with industrial sector classification (Question 1) and regional groupings (Question 2). Industrial sectors particularly provided a choice of basic and precious metallurgy, engineering, food processing, textiles, closing and shoes production, chemical industry, wood processing, construction materials, medicine, paper production and leather processing. Industrial classification, as noted in Section 4.2, included Moscow, the Moscow region, St. Petersburg, Nizhni Novgorod, Ivanovo, Vladimir, Chelyabinsk and the Republic of Tatarstan (though useable responses were obtained only from Moscow, the Moscow Region, Nizhni Novgorod and Ivanovo).

The following question asks for the property form of the enterprise, offering a choice of State, municipal or leasehold enterprises; partnerships/production cooperatives; closed and open joint stock companies; private/individual firms; public organisations; and other property types of the firms. Question 4 intends to establish if the establishment is independent unit or is a part of a larger enterprise.

The next nine questions are related to numerically measurable attributes of the main enterprise activities and resources. Here, the respondents were asked to provide percentage data on shares held by insiders (i.e. workers and managers), the State and foreign owners; sales exported within the CIS, outside the CIS, either for cash or barter; they also disclosed wages, training cost's and social cost's shares of production costs; the total number of workers employed; the number of workers on administrative leave (unpaid,

partially paid, or full paid); and labour turnover within last year (total, resigned and dismissed). The last four numerical questions here address the value of earnings (in thousand roubles) for all employees, and specifically for managers, skilled and unskilled workers. These earnings are also distinguished among average wages paid, amounts paid in the form of bonuses, and the number of benefits provided.

The questions on the share distribution of firms facilitate the important classification of enterprises. As was stated in the Literature Review and Hypotheses Chapter, various CG systems, and specifically different types of shareholders, can have a significant influence on strategic decisions, that subsequently influence performance. Thus, one of the aims of this study is to thoroughly identify insiders' influence on *strategies* through *governance*, and on *performance* through *strategies*.

The next part of the questionnaire begins with general directors being asked to estimate the values of some indicators, by providing mostly "yes", "no" or "do not know" answers to questions, which were later instrumented into binary variables. All of these questions were found to be clearly worded and relevant to general directors' or managers' responsibilities. For example, this set of questions starts with Question 15 on "foreign investments in enterprise", which is next followed by the whole bulk of training-associated questions (Questions 16-22): "initial training"; "retraining to improve job performance"; "providing training to upgrade"; "change in period training program"; "paying for special training institute"; "is paying practice going on now"; or "planning to cut financing the training institute". The data obtained from these "training" questions were required in terms of guidance rather than as real numbers, however their use will allow the identification of various HRM strategies of the enterprises during statistical testing.

The next group of "yes" or "no" questions includes those on "change in volume of production" – Question 23; "effect of product range change on employment" – Question 24; "effect of technological change on employment" – Question 25; and "effect of work organisation change on employment" – Question 26. These four questions are accompanied by the numerically measurable "capacity utilisation rate" (Question 27), asked for as a percentage.

The next group of questions represents a mix of the different types of questions, and addresses the issues of wage determination and forms in which wages are paid. In particular, in Question 28 respondents were offered a multiple choice to specify among enterprise performance, individual performance, minimum wage law, or option "other" for the "main criteria of wage determination". Three subsequent questions were incorporated here to provide numerical answers to the "percentage of workers paid non-monetarily" – Question 29; "percentage of wages paid non-monetarily" – Question 30; and "percentage of wages not paid on time" – Question 31. The respondents were also asked if profit sharing system was operating on their enterprises within the last year (Question 32).

The questions on remuneration system types and benefits provided constitute the next group of surveyed questions. Namely, a multiple choice of: basic wage; basic wage with individual bonuses; basic wage with monthly bonuses; and option "other" was provided for valid types of remuneration system in Question 33. The following question intends to capture the long list of 17 types of benefits provided by enterprises to its employees (ether administrative or regular), accompanied by a choice of five perceptual frequency answers – "yes", "no", "occasionally", "not available" and "do not know". The benefits include (see Appendix I for a full list): paid vacation, rest houses, sickness benefit, paid health services, subsidised rend, subsidised kindergartens, loans, retiring assistance, supplementary pension, etc. Two subsequent questions inquire if any benefits like subsidised catering, subsidised transport, subsidised housing, payment for additional vacation, medical service, medical insurance, social insurance, subsidised kindergarten, vouchers, subsidised prices, profit sharing, financial assistance, "other", or "none" of these were added (Question 36) or excluded (Question 37) within the last year.

The last set of questions addresses the provision of social housing (Question 40), and the maintenance of social facilities (Question 38) or their transfer to local authorities (Question 39). The questionnaire ends with a multiple choice Question 41 on a perceived bankruptcy threat within the next year.

The next four subsections represent main variables and controls, organised from the answers collected during the survey, and comprise Main Independent Variables (4.3.1),

Main Dependent Variables (4.3.2), Composite Strategic Variables (4.3.3) and Controls (4.3.4).

4.3.1 Main Independent Variables

For *Governance – Strategy* estimation, CG variables represent the main independent variables in the estimation of the determination of strategic decisions, and include two sets of influences: ownership proportions and property form variables. Ownership is measured by the percentage of shares held by each type of owner – perhaps the most widely-used approach, e.g. Brown and Earle (2000), Claessens and Djankov (1999a, 1999b), Earle and Estrin (1996, 1997), etc. The four continuous ownership variables were constructed from Questions 5.1 – 5.4, asked regarding a percentage of shares held. These include:

IO – percentage of total managers' and workers' shareholdings, i.e. the percentage of insiders' shares;
MO – percentage of managers' shares;
WO – percentage of workers' (employees') shares;
SO – percentage of State's shares.

In discussing issues of employee ownership it is important to distinguish between ownership and control over the enterprises. Table 6 hereafter shows that insiders represent a majority of owners of Russian privatised enterprises (in the ILO sample). However, for all of the considered enterprises, managers' shareholdings significantly exceed those of workers, which raises the question of workers' power to influence managerial decisions.

As with workers' ownership, managerial share ownership has a Janus face: shares held by managers can provide incentives for improved decision-making directed at shareholder value, but at the same time, MO can facilitate *entrenchment* behaviour by managers, as they wield their shares and voting power to protect their existing jobs, perquisites and power too (Morck *et al.*, 1988). Furthermore, it has been argued that MO can have an exponential influence on incentives and entrenchment. In support of this notion, Morck *et*

al. (1988) find that MO has a positive association with firm performance at low level of MO, but over a higher MO, entrenchment dominates improved incentives. At very high levels of MO, however, senior managers seem to behave like shareholders again. To accommodate this possibility and following Morck *et al.* (1988), the term MO squared (MO^2) will be included in one version of *Governance – Strategy* model (see Subsection 4.6.1 below).

State representation as the owner of privatised Russian firms was noted to decline over years (see Table 1 in Chapter II) and does not present a significant share in our data too (Table 6). To avoid collinearity with ownership proportions adding to unity, one ownership variable had to be omitted. Once it is recognised that privatisation is associated with more enterprise restructuring, and since in the main focus of this research are privatised Russian firms (i.e. inside, outside and privately owned), and considering the available data, the category of State ownership was therefore excluded. When comparing the full model (with SO included) with the restricted one (without SO), the variable deletion test showed no significant contribution from the eliminated variable to the residual sum of squares, thus supporting its omission (Maddala, 1994). The decision to remove SO is also supported by the Djankov and Murrell (2002) analysis of restructuring enterprises in transition economies, which examines the effectiveness of different reform policies and the effects of privatisation. The authors find that state ownership (within traditional state firms) is less effective than all other ownership types.

Besides ownership proportions as CG variables, a set of four legal-form dummies was constructed from a list of questions asked regarding property forms of the considered establishments. In particular, Question 3 of the questionnaire (see Appendix I) proposed a choice of: (1) State, municipal or leasehold enterprises; (2) partnerships/production cooperatives; (3) closed or (4) open joint stock companies; (5) private/individual firms; (6) public organisations; and (7) other property types of firms. The ILO sample contains significant proportions of closed and open joint stock companies (CJSC and OJSC respectively) and partnerships (PART). These dummies equalled one if an enterprise has a particular legal form and zero otherwise. Here, following Djankov and Murrell (2002), a LOGIT (dummy-variable) regression was chosen to test for the effect of property forms on

enterprise strategies, rather than simply using differences between the means of property form proportions.

The analysis of the sample (Table 6), gives the following average sample share distribution for the considered property forms of the enterprises:

Table 6. Sample Average Percentage of Shares

Property Form	Total Insiders	Managers	Workers	State
Partnership	71.38	62.17	7.17	4.41
Closed JSC	87.69	46.05	41.78	2.69
Open JSC	56.41	31.21	25.67	10.65

Note: managers' and workers' shares do not sum to total insiders owing to some companies not distinguishing between different kinds of insider.

Table 6 suggests that differences between owners are of great importance. It shows that managers and workers have significant equity stakes in closed and open JSCs, which means that these two types of owners (especially workers) could have an influence over various (strategic) decisions. At the same time, in partnerships managers' ownership significantly exceeds that of workers. State shareholdings are the smallest in all the considered property forms of the enterprises. This finding will have an application for hypotheses testing of *Governance – Strategy* relations, when the sample will be restricted to only closed and open JSCs (out of the whole sample), i.e. to enterprises where ownership may be expected to change because of high proportions of shares held by private inside owners (Djankov and Murrell, 2002).

For the *Strategy – Performance* analysis firm strategies were represented by independent variables comprising strategies directly. These in particular include "wage share of production costs", "social cost share of production costs", "training share of production costs", training systems introduced (initial training, training to upgrade or general increase in training), "proportion of total range of benefits received" (for administrative and regular

workers), "unpaid leave" and labour turnover parameters, specified by the total number of dismissed within the last year (June 1999 – June 2000).

Many studies have employed training parameters as independent variables for *Strategy – Performance* examination: Bae and Lawler, 2000; Delaney and Huselid, 1996; Fey and Björkman, 2001; Huselid, 1995; Kaplan and Norton, 2001; Koch and McGrath, 1996; MacDuffie, 1995; etc. For instance, Bae and Lawler (2000) use "amount of money spent on training" variable; "opportunity for training"; "extensive training for general skills", "availability of different kinds of training"; "systematically structured training process" and "high priority on training". These researches provide support to the notion that such HRM activity as training are positively associated with company performance, which, in particular, could be achieved though work force motivation and skills improvement.

The variable "proportion of total range of benefits received" was constructed from a list of 17 benefits actually provided for the employees and reported in Questions 34-35 of the questionnaire (see Appendix I). These benefits ranged from paid vacation and sickness benefit through paid health services and subsidised rents, to subsidies for kindergartens and retirement assistance. With the focus of this research on employee welfare we examine average benefits for both administrative workers and regular workers.

There is a prevailing universal assumption that there are always HRM activities that are better than others, and therefore organisations have to adopt these activities (Huselid, 1995; Osterman, 1994; Pfeffer, 1994). In particular, such HRM activity as training has been found to be positively associated with company performance (e.g. see Pfeffer and Veiga, 1999). Consistent with these findings, successful companies (in the US or the UK) put an emphasis on training and other training-focused activities because skilled and motivated work force, that has a knowledge and capability to perform required tasks, is likely to bring competitive advantage to the firm, what also results in profits. In this thesis training was considered in four variables describing initial training, training to upgrade, increase in training and retraining to improve job performance. These variables were also instrumented with two dummies: first equal to one if training was provided and zero otherwise, and will be examined as strategy parameters, resulting in improved performance.

After this introduction of the main independent variables, the next Subsection turns to main dependent variables for this study.

4.3.2 Main Dependent Variables

In testing the established sequence of *Governance – Strategy – Performance*, we firstly use *strategy* variables as dependent during the *Governance – Strategy* stage, and subsequently apply them as independent variables for the *Strategy – Performance* stage.

The analysis of *Governance – Strategy* relationships is focused on a study of the effects that CG parameters like managerial or workers' shareholdings, or legal property forms of enterprises, have on such dependent strategy parameters as "wage share of production costs", "social cost share of production costs", "training share of production costs", training systems introduced (initial training, training to upgrade, retraining to improve job performance and increase in training), introduction of remuneration system in the form of basic wage with monthly bonuses, "proportion of total range of benefits received", and labour turnover parameters.

In addition to variables specified in the previous Subsection, it is worth mentioning that remuneration system variables for *Governance – Strategy* estimation were constructed in the form of basic wages paid together with monthly bonuses. This variable was instrumented with two dummies: first equal to one if the described remuneration systems was provided and zero otherwise.

For examining the implications of managerial *strategies* for firm *performance*, researchers usually use accounting measures and ratios. However, unfortunately this is not possible in case of Russia (Hoskisson *et al.*, 2000) where the national accounting system is different from the international one and only few (mostly internationally traded) companies follow international standards or use both systems. Also the unwillingness of firms to provide tax authorities with true data and imperfect disclosure codes make performance indicators rather unreliable, so the use of such stock market performance indicators as Tobin's Q, or

other variables that are performance measures of companies in market economies, is not feasible for Russia. Also, a significant number of papers measure performance in output level, captured, for example, by sales (e.g. Konings, 1997; Earle, 1998); added value (Anderson *et al.*, 2000; Smith *et al.*, 1997); or growth rates of revenues, employment, revenues per employee, and costs per unit of revenue (Frydman *et al.*, 1999; Jones, 1998). However, these measures were intentionally not asked during the survey process, to prevent non-responses and total avoidance of participation (Standing and Zsoldos, 2000).

The problems associated with a lack of comprehensive performance data could be overcome with the introduction of a number of proxies for performance that describe both positive and negative sides of it. Among the positive performance indicators are "increase in volume of production", and numerically measured "percentage of sales exported within the CIS", "percentage of sales exported outside the CIS", and average capacity utilisation during the year.

The choice of export variables as the proxies for performance is supported by Earle *et al.* (1996) and later by Filatotchev *et al.* (2001b), who find that, for employee-owned and outsider-owned firms in Russia, exports are significantly higher than in firms with other forms of ownership. The authors focus on exports as a percentage of total sales, as a key strategic performance outcome, and show that while ownership structure has an insignificant direct association with performance, governance affects mediate strategies that in turn are related to performance. In particular, *MO* was found to be positively related to product strategies (through quality control) that focused rather on domestic than export markets. These findings on associations between *MO* and export-oriented strategies support the use of percentage of sales exported as a measure of performance.

There is also some evidence (Driver and Thompson, 2002) that downsizing programs of corporations in recent years have caused macro-level short-term damage to the economies in which they took place because of the extensive cut-backs of investments, which subsequently damaged their performance. However, some scholars argue (for the US, see Donaldson, 1995; and Shleifer and Vishny, 1997) that a downsizing strategy was chosen deliberately to improve performance by reducing investments. Similar literature for the UK shows that MBOs combined cost cutting with increases in efficiency investments

(Thompson and Wright, 1995; Wright *et al.*, 1992). On the one hand, this may be explained by existing low levels of equipment per worker, although on the other hand, the effect may have been to reduce capacity utilisation (Driver and Thompson, 2002). Following this experience, we introduce an average capacity utilisation (during the year) as a proxy for performance.

Negative performance indicators included numerically measured "percentage of sales bartered", "the percentage of wages paid non-monetarily", and binary ("yes", "no" or "do not know") perceived bankruptcy threat in the next 12 months.

With the prominence given to Kornai's (1990) concept of the relatively soft budget constraint under socialism, it seems strange that so little emphasis in the Western *Governance – Strategy – Performance* literature or the literature on economic transition has been placed on the penalties for poor performance. In this context, it is actors' perceptions and expectations of negative phenomena (such as the bankruptcy threat or non-cash sales) that may be expected to influence attitudes towards HRM policies. This study may claim some novelty in its design and application of negative performance indicators like perceived bankruptcy threat. Thus, this thesis also endorses and extends the view of Fey and Björkman (2001), who argue the case for subjective performance measures.

4.3.3 Composite Strategic Variables

It was noted that to date there was only one large-sample empirical study by Buck *et al.* (2003) on the influence of governance forms on HRM strategies in the FSU, specifically Ukraine. Other research was performed by Fey and Björkman (2001), limited to the *Strategy – Performance* aspect of foreign subsidiaries operating in Russia. This thesis intends to embrace the whole *Governance – Strategy – Performance* relationship in indigenous Russian firms by examining three composite business policy variables (based on theoretical expectations) representing *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* strategies.

Given the range of models and methodologies for specific HRM bundles, research in Western or CEE countries (e.g. see the summary table in Subsection 3.3.4 of Chapter III), and following the introduced methodology for modelling specific HRM strategies in Russian firms (Subsection 3.3.1 – 3.3.3 *ibid*), this Subsection introduces variables that were clustered into the three coherent HRM bundles – *TSW*, *CM* and *HRI*.

However, Ngo *et al.* (1998) point out that there is only limited theoretical guidance on precisely how HRM practices should be bundled together. Therefore, in choosing appropriate clusters for the three coherent HRM bundles in this research, we follow Baron *et al.* (1996, 1999); Hannan *et al.* (1996); Berger and Huselid (1996); MacDuffie (1995); Osterman (1999, 2000; Spenner *et al.* (1998), and conceptualise the constructs according to established theoretical expectations.

Since direct observations for most of elements of the three bundles were not available in the same units of measurement (Delaney and Huselid, 1996), we constructed the following proxies from the relevant 26 responses in the questionnaire for the three composite business policy variables representing *TSW*, *CM* and *HRI* strategies. For each of the specified HRM bundles they include:

Traditional Social Welfare (TSW)	
High wage share of production costs	Question 7.1
High social costs share of production costs	Question 7.2
High proportion of full or partially paid workers on administrative leave	Questions 9.2-9.3
Firm provides initial training	Question 16
High proportion of total range of benefits received	Questions 34-35
No social benefit was excluded during the last year	Question 36
Firm maintains social facilities	Question 38
Firm provides housing services	Question 40

Cost Minimisation (CM)	
Low social costs share of production costs	Question 7.2
High proportion of dismissed employees	Question 10.3
Firm reduced training	Question 19
Firm did not pay or plan to reduce paying for training	Questions 21-22
Firm introduced new product range, work organisation or technology resulting in reduction of employment	Questions 24-26
Individual performance was a main criterion of wage determination	Question 28
High proportion of wages paid non-monetarily	Questions 30.1-30.2
Low proportion of total range of benefits received	Questions 34-35
At least one new social benefit was excluded during last year	Question 37
Firm transferred social facilities to local authorities	Question 39

Human Resource Investment (HRI)	
Firm provided training to improve job performance	Question 17
Firm provided training to upgrade (to raise pay and obtain a higher grade)	Question 18
Firm provided funds for special training institute and grants	Question 20
Firm introduced new technology resulting in increase or no change in employment	Question 25
Firm introduced new work organisation resulting in increase or no change in employment	Question 26
Team performance was a main criterion of wage determination	Question 28
Firm had a profit sharing system (profit related pay)	Question 32
At least one new social benefit was added during last year	Question 36

Some of the variables that were combined into composite variables above, were continuous, and some were nominal ("yes", "no" or "do not know" responses). For continuous variables, sample means were used as cut-off points to define "high" and "low" levels of variables. A strong *TSW* strategy (or weak for *CM*) was identified with a high proportion of total range of benefits received variable, a count of responses was used to evaluate the presence of individual social benefits (e.g. paid vacation, sickness benefit

through paid health services, subsidised rent and subsidies for kindergartens, retirement assistance, etc.) to provide a measure of the proportion of total social benefits actually provided. All variables were then dichotomised into nominal variables. Finally, each HRM cluster was constructed as a linear combination of the unweighted means of the relevant outcomes for the corresponding HRM strategy.

This approach of constructing composite measures prevented us from getting a mixture of dichotomous and ordinal measures in HRM bundles, and thus precluded this approach from extreme degree of non-normality, exhibited usually in survey data (Delaney and Huselid, 1996; Nunnally and Bernstein, 1994). A detailed description of confirmatory cluster analysis and its results are presented in Subsection 4.4.4 and Section 5.5 below.

4.3.4 CONTROLS

A variety of control variables, supplementing the proposed influence of *governance* on *strategies* and subsequently of *strategies* on *performance* (related to employee welfare), were employed to hold non-hypothesised influences constant. These controls are common and include (employment) size of the enterprise, industrial sector dummies, firm as "part of a larger enterprise" dummy and "foreign investment in the enterprise" dummy.

Many researches use industrial sector dummies as controls: for instance Djankov and Murrell (2002) in their enterprise restructuring in transition quantitative survey. The use of industrial sector dummies (*IND*) is supported by the fact that labour markets in Russia are highly compartmentalised industrially and it often happens that wages set by a (large) industrial firm have an impact on wages set by other firms and on wage setting in the region. Food and Light industries, Chemistry, Wood & Paper, and industry of Construction Materials present industrial sectors from Moscow and Moscow Region, Nizhni Novgorod and Ivanovo. "Part of a larger enterprise" is also a very common control parameter. It could discover the nature of the product competitiveness or provide an insight to establishment's skills level of the work force (Osterman, 2000).

Enterprise *SIZE* was also controlled for, since larger firms might have more resources to devote to business generally and to HRM investments in particular. *SIZE* is measured here as the logarithm of absolute number employed (Koch and McGrath, 1996) so that a few large firms would not disproportionately affect results.

These control variables were used for investigation of the proposed *Governance – Strategy* and *Strategy – Performance* relations in terms of human resource strategies.

4.4 Statistical Techniques

4.4.1 Statistical Assumptions for Econometric Models

A regression model must be correctly specified in terms of the proposed functional form and variables included in the model. The majority of regressions utilise the OLS type of regression model, which is one of the most common statistical methods for estimating the values of constant α and regression coefficients β of multiple linear regression models, expressed in the general form of $Y_i = \alpha + \beta X_i + \varepsilon_i$, where Y_i is the i^{th} true dependent variable, X_i is the i^{th} true independent variable, and ε_i is a random error term.

Multiple regression models have more than one independent variable (X_i) and imply a number of important assumptions for model specification, independent parameters and the error term. To be able validly to apply the OLS model to the data and be able to test the relationship between the variables, the data must comply with the assumptions underlying the regression model (Watsham and Parramore, 1997). For the error term ε_i, the following assumptions apply:

- The error term has a zero mean for any given value of X_i implying that the estimated value of Y_i, $\hat{Y}_i$, for any given X_i is equal to $\hat{\alpha} + \hat{\beta} X_i$, where estimated values of α and β are denoted by $\hat{\alpha}$ and $\hat{\beta}$

- The variance of ε_i for each X_i is a constant σ^2, known as the assumption of heteroskedasticity (i.e. if the variance of ε_i changes with X_i, then it is referred to as heteroskedasticity)
- The random error terms associated with two different observations are uncorrelated, i.e. there is no autocorrelation between the error terms (covariance between pairs of error terms is zero)
- The error term is normally distributed for each X_i
- The error has zero covariance with each explanatory variable

For a basic examination of *Governance – Strategy* and *Strategy – Performance* relations the following two multivariate estimating equations were used, based on the multiple linear regression equation above:

$$R_{G\to S} = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \ldots + \beta_n X_n + \varepsilon$$

$$R_{S\to P} = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \ldots + \beta_n X_n + \varepsilon$$

These regressions (presented here in general form) and their variations for strategic bundles will be explained in full detail later in this thesis, together with the independent variables included for each approach (Section 4.6). Here, it is worth noting, that $R_{G\to S}$ and $R_{S\to P}$ represent dependent strategy and performance variables respectively.

LOGIT models extend the principles of generalised linear models (regressions) to better treat the case of dichotomous dependent variables and differ from standard regression by substituting the maximum likelihood estimation of a link function of the dependent variable for regression's use of least squares estimation of the dependent variable itself. The function used in LOGIT is a natural logarithm of the odds ratio. The odds ratio is the ratio of the probability that something is true divided by the probability that it is not, i.e. $LOGIT = \ln\left(\frac{P}{1-P}\right)$ where $P = \Pr(\text{variable} = 1)$ if the event occurs or equals zero otherwise. LOGIT models contain exactly the same information as odds ratios (that is,

they are measures of the strength of relationship between variables) but because they are symmetrical, they can be compared more easily. A positive LOGIT means the independent variable has the effect of increasing the odds that the dependent variable equals a given value (usually 1 for binary dependents and usually the last value for multinomial dependents). A negative LOGIT means the independent variable has the effect of decreasing the odds that the dependent variable equals the given value.

Following the above description, the general form of the LOGIT model (for binary variables) for the examination of *Governance – Strategy* relations is presented by the equation:

$$LOGIT(R_{G\to S}) = \ln\left(\frac{R_{G\to S}}{1-R_{G\to S}}\right) = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \ldots + \beta_n X_n + \varepsilon$$

$R_{G\to S}$ represents dependent strategy variables respectively here. As with the OLS multivariate regressions described above, Section 4.6 will explain in full detail all variations of LOGIT models for testing *Governance – Strategy* and *Strategy – Performance* relations, together with the independent variables included for each approach.

4.4.2 Examination of Regression Parameters

To evaluate goodness of fit of the regression equation, the coefficient of determination R^2 is calculated. To calculate it, we need to find the total sum of squares (SST), the sum of squares due to regression (SSR) and the sum of squares due to error (SSE).

Following Watsham and Parramore (1997), SST is the sum of the squared differences between observed value of the dependent variable Y_i and the mean of the observed values of the dependent variable $\bar{Y}$, i.e. $SST = \sum (Y_i - \bar{Y})^2$. The SSR is the sum of the squared differences between the predicted values of the dependent variable $\hat{Y}_i$ and the mean of the

observed values of the dependent variable $\overline{Y}$, i.e. $SSR = \sum(\hat{Y}_i - \overline{Y})^2$. And finally the SSE is the sum of the squared differences between $\hat{Y}_i$ and Y_i, i.e. $SSE = \sum(Y_i - \hat{Y}_i)^2$.

The SST equals the sum of SSR and SSE. The SSR/SST ratio gives the proportion of the variation in Y explained by the variation in X. This ratio is called the coefficient of determination and is defined by R^2.

The coefficient of determination is calculated as $R^2 = \frac{SSR}{SST} = \frac{\sum(\hat{Y}_i - \overline{Y})^2}{\sum(Y_i - \overline{Y})^2}$

R^2 varies from zero (if X has no influence on Y, i.e. predicted value Y_i is not better than the mean value $\overline{Y}$) to one (if variation in X explains all the variation in Y, i.e. $\hat{Y}_i$ perfectly predicts Y_i). Therefore, the larger the value of the coefficient of determination, the better the fit. However, in cross-section studies a lower level of R^2 could happen because of the large variation across individual observations, inherently presented in the data (Pindyck and Rubinfeld, 1981), but the model will still be satisfactory.

In the multivariate regression model, the addition of new explanatory variables causes the coefficient of determination to increase. So, instead of using R^2, the adjusted coefficient of determination $\overline{R}^2$ has to be used to take account of the number of independent variables (Watsham and Parramore, 1997).

$\overline{R}^2$ is calculated as $\overline{R}^2 = 1 - (1 - R^2)\frac{n-1}{n-k}$, where n is total number of observations and k is the number of explanatory variables. The adjusted coefficient of determination will decrease if a new added variable is not significant, but the decision on adding or deleting variables has not to relay on their influence on adjusted R^2 only. The main basis for inclusion/deletion is the theory behind the regression that is being tested, so a "variable that has a strong theoretical basis for inclusion should be added to the regression even if the adjusted R^2 fails to improve" (Watsham and Parramore, 1997, p.204).

Another useful statistical indicator is the significance of the regression model. Under the basic (null) hypothesis, it is implied that each of explanatory variables X_i has no effect on the dependent variable Y, or the effect of all explanatory variables X_is together is jointly zero, i.e. $\beta_1 = \beta_2 = ... = \beta_i = 0$. The alternative to the null hypothesis is that at least one of the explanatory variables X_i affects Y, i.e. $\beta_1 \neq \beta_2 \neq ... \neq \beta_i \neq 0$. If the designed regression model has a high explanatory power, the variation in the dependent variable Y will be caused by variations in the independent variables X_i and the sums of squares due to regression (SSR) will be large relative to the sum of squares due to error (SSE). If, on the other hand, the model has low explanatory power, the variations in the dependent variable Y will be caused by variation in the error term, and the SSE will be large relative to the SSR (Watsham and Parramore, 1997).

The test statistic for R^2 is calculated as $F \sim \frac{R^2 / k}{(1-R^2)/(n-k-1)}$, where F follows the F-distribution with k and n - k - 1 degrees of freedom[2]. If the calculated value of F is greater than the critical value, then statistical significance of the model is concluded (via the rejection of the null hypothesis).

To check if each of the regression coefficients is significantly different from zero, we need to calculate t-statistics, by dividing estimates of the regression coefficients by the estimated standard errors.

The t-statistic is t-distributed with n - k - 1 degrees of freedom and is represented as $t = \frac{\hat{\beta}_i}{S_{\hat{\beta}_i}}$, where $\hat{\beta}_i$ is the estimated value of β_i and $S_{\hat{\beta}_i}$ is its estimated standard error. The regression coefficients are significant when t-statistics are greater than their critical values (Watsham and Parramore, 1997).

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[2] The test statistic for adjusted R^2 is calculated as $F_{k-1,n-k} \sim \frac{R^2}{(1-R^2)} \frac{(n-k)}{(k-1)}$, where the test statistic is F-distributed with k - 1 degrees of freedom in the numerator and n - k degrees of freedom in the denominator (Watsham and Parramore, 1997).

4.4.3 MODIFICATIONS OF REGRESSION MODELS

To test the eight main hypotheses stated above, a number of diagnostics had to be performed. Data were analysed using a number of formal tests, using moderated regression analysis. The latter shows the presence of heteroskedasticity, confirmed by Breusch-Pagan tests, so Huber/White/sandwich modifications of OLS and LOGIT were chosen for continuous (e.g. insider share ownership proportions), categorical (e.g. legal form of enterprise) and binary variables (e.g. responses to the questions like "were new social benefits introduced?").

If the residuals have a constant variance, they are homoskedastic, but if the variance is not constant, then residuals are heteroskedastic. Heteroskedasticity implies that the regression coefficients are no longer the best (or minimum) variance estimates, i.e. they are no longer the efficient estimators. So, although the coefficients are unbiased in the regression, the variance and the standard errors of these coefficients will be biased. Thus, it is possible to accept the hypothesis when in fact it should be rejected.

As a solution to heteroskedasticity, the relationship between the error terms has to be examined, and then the regression model has to be transformed to reflect this relationship. In particular, this may be achieved by regressing the error term on different functional forms of the variable that causes the heteroskedasticity (Watsham and Parramore, 1997).

The Breusch-Pagan test computes the Breusch-Pagan (1979) Lagrange multiplier for heteroskedasticity in the error terms, conditional on a set of variables which are presumed to influence the error variance. The test statistic, a Lagrange multiplier measure, is Chi-square distributed under the null hypothesis of homoskedasticity (Breusch and Pagan, 1979). Breusch-Pagan test is asymptotically equivalent to White's (1980) general test for heteroskedasticity (Greene, 2000), which tests for heteroskedasticity in the error distribution by regressing the squared residuals on all distinct regressors, cross-products, and squares of regressors.

In the case of a LOGIT model, the introduction of a *robust* or *cluster* command for maximum likelihood estimation gives the Wald test (statistics) of a Chi-square test, rather than a likelihood-ratio test. A Wald test is used to test the statistical significance of β coefficients in LOGIT model and is calculated by Z-statistics ($Z = \frac{\beta}{SE}$), then squared and yielding a Wald statistic with a Chi-square distribution[3]. SE represents a standard error of regression coefficients. However, Menard (1995) warns that for large coefficients, the standard error is inflated, lowering the Wald statistic (chi-square) value.

4.4.4 Cluster Analysis

To examine the total HRM system, and to develop and empirically identify key dimensions of a firm's HRM system, cluster analysis was deployed.

Cluster analysis is a multivariate statistical tool that can be used to examine associations or the underlying relations among a large number of variables and to determine if it is possible to summarise the information into a smaller set of composite variables (Cool and Henderson, 1997). Cluster analysis can be both an explanatory and a confirmatory. In explanatory cluster analysis, no *a priori* constraints are imposed on the number of generated bundles, while in confirmatory cluster analysis, the researcher has some predetermined ideas, based on previous research, about the actual structure of data and the number of bundles (Hair *et al.*, 1995).

Following Cool and Henderson (1997), when a questionnaire is designed a for confirmatory cluster analysis, similar questions are usually asked in order to form a multi-subject construct. However, the idea with the ILO questionnaire was to cover a large

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[3] In fact, Chi-square statistic is quite similar to F-statistics after a normalisation: Chi-squared = (numerator degrees of freedom) * F. Chi-square is the limiting distribution of the F, as the denominator degrees of freedom go to infinity (Gould, 1999).

number of firms, getting multi-subject responses from them. So the questionnaire was not designed for confirmatory cluster analysis.

The preceding theoretical discussion (see Chapter III) of specific *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* strategies identified a reasonably broad variety of HRM strategies in the literature. It was also noted by some researchers (Osterman, 1987; Pfeffer, 1994), that HRM systems, rather than individual practices, are the appropriate level of analysis when an estimate of the firm-level effect of HRM practices is desired. In particular, it is known that HRM practices may cause studies, which focus on a single practice at a time, to overestimate its contribution to enterprise performance because of collinearity among these practices (Delaney and Huselid, 1996). At the same time, studies that embrace multiple HRM measures could also underestimate the effects of these practices, but in different ways. First of all, collinearity among HRM variables increases standard errors and reduces likelihood that individual HRM coefficients will be statistically significant. Then, studies could underestimate the combined firm-level effect of the multiple measures to the extent that complementarities exist among HRM practices (Huselid, 1995; MacDuffie, 1995). This led researchers to employ data reduction procedures, like cluster analysis and factor analyses (Huselid, 1995; Youndt *et al.*, 1996), to create bundles of clusters.

Following MacDuffie (1995), there are three statistical procedures, each confirming advantages and disadvantages, that can be used to validate "bundle": reliability analysis, factor analysis and cluster analysis. Reliability analysis can evaluate the intercorrelations among variables grouped together into a bundle – an advantage if the conceptual basis is strong for categorising practices, and a disadvantage if not. Factor analysis is more appropriate for the identification of interrelationships among sets of items in scale, all designed to measure the same conduct. Factor analysis is less appropriate for assessing a bundle, which is not a scale, but an index, consisting of the set of interrelated variables (DeVellis, 1991), each of which represents a different parameter. Cluster analysis groups observations that lie in close proximity in multidimensional space for a given set of variables. Since different clustering algorithm produce different clusters, it is important to test if obtained clusters are quite distinctive (Hartigan, 1995; Ulrich and McKelvey, 1990).

With dozens of HRM strategy elements in the survey questionnaire, simplification was achieved through cluster analysis which seeks to identify homogenous subgroups of cases from the sample data. In other words, cluster analysis (also known as segmentation analysis), seeks to identify a set of groups, which both minimise within-group variation and maximise between-group variation (Garson, 2001). For these purposes three composite business policy variables (strategic bundles) were generated from the relevant responses in the questionnaire (reported in Subsection 4.3.3 above), and then methods of k-means cluster analysis and stepwise discriminant analysis were used together with ANOVA and Chi-square tests for validation of each composite strategy variable.

However, before discussing the results, it is also important to acknowledge a legitimate concern that associations between main independent and dependent variables could be attributable to common methods bias. This implies that variables in this study may be correlated because of common method variance derived from data, being collected from the same respondents (De Jong and Kemp, 2003).

There are a number of approaches to test for potential common method bias. Some authors (e.g. Tanewski *et al.*, 2003) follow principal-axis factor analysis (Podsakoff and Organ, 1986) accompanied by Kaiser criterion for retention of factors. Others (e.g. De Jong and Kemp, 2003) check for common method variance using Harman's (1967) one-factor test. To demonstrate the independence among conceptual clusters, comprising the three strategic bundles, we use principal-axis factor analysis. In particular, this analysis involves the factor analysis of independent and dependent variables, and extracting the first factor, which should contain the best approximation of common method variance (Podsakoff and Organ, 1986).

The result of the performed principal-axis factor analysis allows us to conclude that common method variance bias is not a threat to the validity of this thesis. Further techniques used in this research for validation of the three strategic bundles of clusters, and results of the described methods of cluster analysis, are presented in Section 5.5 below, and in the Appendix II.

4.5 SIMPLIFICATIONS FOR CROSS-SECTIONAL APPLICATION

The objective of most cross-sectional surveys is to produce unbiased (or fairly unbiased) estimates of levels such as totals or means at a given time point. However, one of the limitations of this study (all limitations will be thoroughly examined together in a later Section) is its cross-sectional nature, which requires caution in drawing causal inferences, while some relationships may be susceptible to reverse causality. Thus, a distinction has to be made between cross-section analysis and time-series analysis. Following Watsham and Parramore (1997), cross-sectional regression tests the relationship between variables at a particular point of time, while for time-series data for each variable is collected over successive time periods.

The McConell and Servaes (1990) and Holderness *et al.* (1999) papers, which use data from two different years and test the predictions on both sets, are exceptions to the overall pattern of using a cross-section of data at only one point in time. The approach of this research, which is actually due to limited data availability, cannot establish the associations between *governance*, *strategy* and *performance* over time and is based upon one cross-section of data for the year 2000, which nevertheless provides a rich variation in parameters.

Once CG mechanism is not the only source of value creation in firms, a theoretical prediction of the *Governance – Strategy – Performance* interaction should therefore include exogenous variables in the environment, that either influence *governance* directly or affect *performance* without influencing *governance* (Bøhren and Ødegaard, 2001). The problem is, however, that with complications like conflicts of interest between managers and owners, no existing valuation model can specify these characteristics, and the standard solution to this problem is an ad-hoc approach, which is used to explain cross-sectional differences, i.e. factors which have been shown to have independent explanatory power on governance/strategy, and thus have to be included in regression models.

In terms of these examinations, the approach adopted in this work, uses ownership shares of insiders (i.e. of managers and workers), legal forms of the enterprises (open and closed

JSC and partnership) and *TSW*, *CM* and *HRI* composite bundles as independent measures of *governance* and *strategies*. Consistent with the studies of firm ownership structures, the associations between ownership proportions and governance/strategy/performance are examined in a cross-section of firms, rather than on changes in these characteristics between years, although performance is very hard to measure in Russia because of hyperinflation, poor and inconsistent accounting practices, lack of familiarity with developed market definitions of profits, imperfect disclosure codes, etc.

Control variables have also been used to avoid spurious correlations[4]. This problem occurs when an association between *governance* and *strategy* or *strategy* and *performance* is driven by an omitted (third) variable. For example, where (a) performance decreases with firm size as a result of diseconomies of scale, and (b) insider ownership decreases with firm size as a result of the cost of being undiversified, then if performance is regressed on insider holdings alone, a spurious negative relationship between the two variables may in fact be caused by changes in firm size. But if this negative relationship still exists after the size effect on performance has been properly controlled for, insider ownership may have a separate (size-independent) association with firm performance (Bøhren and Ødegaard, 2001). The introduction of size, industry and part of the larger enterprise controls was aimed to prevent the described distortions.

4.6 MODELS AND SPECIFICATIONS

It is recognised by some researches that it is rather difficult to estimate associations between *governance*, *strategy* and *performance* using multivariate regression on one cross-section of data (MacDuffie, 1995). However, Structural Equation Model (SEM) estimation techniques, using LISREL (Jöreskog and Sörbom, 1999), PLS, AMOS, EQS,

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[4] Spurious regression may result from analysing data where the magnitude of the observations of each variable tends to increase (or decrease) over time. This tendency, mostly typical of time-series analysis, creates a degree of correlation that overstates any underlying causal relationship (Watsham and Parramore, 1997).

MPLUS or other software packages, have their own limitations, which made them inappropriate for this research (Fey *et al.*, 2000).

Following Fey *et al.* (2000), there are arguments that favour the use of multivariate regressions. In particular, whereas most of studies have evaluated HRM practices for one entire firm or one selected group of employees only (e.g. see Longenecker and Popovski (1994) study on managerial trials in St. Petersburg's organisations; research of May *et al.* (1998) on Russian HR managers in 31 firms across Russia; or Shekshnia's (1998) paper on HR management in Russian subsidiaries of Western firms; etc.), this thesis studies *Governance – Strategy – Performance* relationships and associated HRM practices separately for managers and workers in Russian industrial firm. To test the first two general hypotheses concerning HRM strategies and subsequent firm performance (see Section 3.2 above), a number of models were constructed for OLS and LOGIT regressions. In particular, the association between CG variables and *strategies* was tested with heteroskedasticity-adjusted OLS estimators. In the case of *Strategy – Performance* associations, adjusted OLS estimators for continuous measures of performance, and LOGIT for binary variables were deployed. For this, we used single-item measures, which prevented us from being able to analyse the data with SEM techniques. However, they did enable us to perform this research on one of the largest samples ever reported for any Russia-focused research (Fey *et al.*, 2000).

One of the weaknesses of "traditional" multivariate regression techniques, emphasised by SEM advocates, is that "traditional" approaches do not take into account of the fact that, for example, causality between *strategies* and *performance* may run in both directions (Hagedoorn and Schakenraad, 1994). However, while *performance* can have a reciprocal causation with *strategy*, *strategy* can not have any reciprocal influence on ownership (in terms of opposite direction to the discussed *Governance – Strategy* relationship). Such unsophisticated SEM modelling will provide results and conclusions that can be seriously flawed and invalid.

Ridgon (1998) discusses various limitations of SEM and maintains that this methodology is still under development. In particular, the author stresses that SEM requires much larger samples than are needed for more specialised methods, such as regressions. The ILO

sample of 295 firms is below the accepted minimum here. Also, Ridgon (1998) points out that all aspects of SEM modelling must be directed by theory, and if not, clear misapplication can occur when data are modelled by SEM, and only then can theory be developed from the analytic results.

Thus, following Fey *et al.* (2000); Knoke (2004); Ridgon (1998) one could see that the price paid for SEM advantages is susceptible to erroneous parameter estimates and model fits if the researcher misspecifies the true measurements and structural relationships. For example, covariation in cross-sectional data offers no clues to asymmetric or reciprocal causation. Also, the temporal sequences among repeated measures in longitudinal panels are not an infallible guide to causal order. (For additional critiques of SEM methods see Cliff (1983) and Breckler (1990).)

According to the above discussion, therefore, it was decided to follow Baron *et al.* (1996, 1999), Hannan *et al.* (1996), MacDuffie (1995), Osterman (1999, 2000), Spenner *et al.* (1998), etc. to perform the analysis of hypotheses developed earlier in this thesis with multivariate regressions, leaving causal modelling techniques for future studies (e.g. on time series of data).

4.6.1 GOVERNANCE – STRATEGY MODELS

To examine *Governance – Strategy* relations in open and closed JSCs, regression equation [1] on insider equity and firm strategies was constructed for continuous data, together with a described modification (see Subsection 4.3.1) with MO squared included [2]. Thus, the first equation is:

$$R_{G\to S} = \alpha + \beta_1 MO + \beta_2 WO + \beta_3 PLE + \beta_4 SIZE + \beta_5 IND_1 + \beta_6 IND_2 + \beta_7 IND_3 + \\ + \beta_8 IND_4 + \beta_9 IND_5 + \varepsilon \qquad [1]$$

where α – constant;

βs – regression coefficients;

ε – error term;

$R_{G\to S}$ – one of dependent strategy variables;

MO – percentage of managers' shares;

WO – percentage of workers' shares;

PLE – part of larger enterprise;

SIZE – size of the enterprise, measured as a logarithm of absolute number employed;

IND_1 - IND_5 – industrial sector dummies, representing Food, Light, Wood & Paper, Chemistry and the Construction Materials industry.

With the addition of the MO squared variable:

$$R_{G\to S} = \alpha + \beta_1 MO + \beta_2 MO^2 + \beta_3 WO + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \beta_7 IND_2 + \\ + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \qquad [2]$$

where $R_{G\to S}$ is one of the dependent strategy variables;

MO^2 – is a quadratic term representing the percentage of managers' shares squared.

Among the dependent strategy variables $R_{G\to S}$ are proportion of total range of benefits received for administrative and regular workers, wage share of total production costs and labour turnover parameters.

To reveal the association between various legal ownership structures and firm strategies, the following equation is estimated for continuous data:

$$R_{G\to S} = \alpha + \beta_1 PART + \beta_2 CJSC + \beta_3 OJSC + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \beta_7 IND_2 + \\ + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \qquad [3]$$

where $R_{G\to S}$ is one of dependent strategy variables;

PART – partnership dummy;

CJSC – closed JSC dummy;

OJSC – open JSC dummy.

Dependent strategy variables $R_{G\to S}$ include proportion of total range of benefits received for administrative and regular workers, wage share of total production costs, social cost share of total production costs and training share of total production costs.

To estimate the relationship between *governance* and *strategy* for binary variables, logistic regression modifications of equations [1], [2] and [3] are deployed. LOGIT is the logarithm of the odds ratio, i.e. $LOGIT(R_{G\to S}) = \ln\left(\frac{R_{G\to S}}{1-R_{G\to S}}\right)$ where $R_{G\to S} = \Pr(\text{variable} = 1)$ if the event occurs or equals zero otherwise. Thus for binary variables, equations [1], [2] and [3] are presented in the form of the following logistic equations:

$$LOGIT(R_{G\to S}) = \alpha + \beta_1 MO + \beta_2 WO + \beta_3 PLE + \beta_4 SIZE + \beta_5 IND_1 + \beta_6 IND_2 + \\ + \beta_7 IND_3 + \beta_8 IND_4 + \beta_9 IND_5 + \varepsilon \qquad [4]$$

And its modification with a term of MO squared:

$$LOGIT(R_{G\to S}) = \alpha + \beta_1 MO + \beta_2 MO^2 + \beta_3 WO + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \\ + \beta_7 IND_2 + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \qquad [5]$$

Among the dependent strategy variables $R_{G\to S}$ are remuneration system in the form of basic wage with monthly bonuses, initial training, training to upgrade, increase in training and retraining to improve job performance.

The association between various legal ownership structures and firm strategies for binary variables is estimated using the following logistic regression:

$$LOGIT(R_{G\to S}) = \alpha + \beta_1 PART + \beta_2 CJSC + \beta_3 OJSC + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \\ + \beta_7 IND_2 + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \quad [6]$$

where the dependent strategy variables $R_{G\to S}$ are presented by layoffs, remuneration system (basic wage with monthly bonuses), initial training, training to upgrade, increase in training and retraining to improve job performance.

4.6.2 STRATEGY – PERFORMANCE MODELS

For examination of the *Strategy – Performance* link, the next equation is used:

$$R_{S\to P} = \alpha + \beta_1 WSPC + \beta_2 SCSPC + \beta_3 TSPC + \beta_4 ABAW + \beta_5 ABRW + \beta_6 FI + \beta_7 IT + \\ + \beta_8 TU + \beta_9 INCT + \beta_{10} UL + \beta_{11} LO + \beta_{12} SIZE + \beta_{13} PLE + \beta_{14} IND_1 + \beta_{15} IND_2 + \quad [7] \\ + \beta_{16} IND_3 + \beta_{17} IND_4 + \beta_{18} IND_5 + \varepsilon$$

where $R_{S\to P}$ is one of the dependent performance variables;

WSPC – wage share of total production costs;

SCSPC – social cost share of total production costs;

TSPC – training share of total production costs;

ABAW – average benefits for administrative workers;

ABRW – average benefits for regular workers;

FI – foreign investment in enterprise;

IT – initial training;

TU – training to upgrade;

INCT – increase in training;

UL – unpaid leave;

LO – layoffs.

Dependent performance variables $R_{S\to P}$ are represented by percentage of sales exported within the CIS, percentage of sales exported outside the CIS, capacity utilisation and increase in volume of production, as positive performance indicators, and percentage of wages paid non-monetarily, percentage of sales bartered and bankruptcy threat, as negative performance indicators.

The increase in the volume of production and the bankruptcy threat are binary variables and require logistic regression for analysis, thus the following modification of equation [7] is used:

$$LOGIT(R_{S\to P}) = \alpha + \beta_1 WSPC + \beta_2 SCSPC + \beta_3 TSPC + \beta_4 ABAW + \beta_5 ABRW + \beta_6 FI + \\ + \beta_7 IT + \beta_8 TU + \beta_9 INCT + \beta_{10} UL + \beta_{11} LO + \beta_{12} SIZE + \beta_{13} PLE + \\ + \beta_{14} IND_1 + \beta_{15} IND_2 + \beta_{16} IND_3 + \beta_{17} IND_4 + \beta_{18} IND_5 + \varepsilon \qquad [8]$$

4.6.3 Composite Strategy Models

Subsequently, a number of hypotheses are generated concerning composite HRM approaches in relation to *governance*, *strategy* and *performance*. The analysis of the stated *Hypothesis 3 – Hypothesis 8* is done through the following four regression equations. For examination of the *Governance – Strategy*, the next two equations are used:

$$R_{G\to S}^{Comp} = \alpha + \beta_1 MO + \beta_2 WO + \beta_3 PLE + \beta_4 SIZE + \beta_5 IND_1 + \beta_6 IND_2 + \beta_7 IND_3 + \\ + \beta_8 IND_4 + \beta_9 IND_5 + \varepsilon \qquad [9]$$

and

$$R_{G\to S}^{Comp} = \alpha + \beta_1 PART + \beta_2 CJSC + \beta_3 OJSC + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \beta_7 IND_2 + \\ + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \qquad [10]$$

where $R_{G\to S}^{Copm}$ are one of the strategy variables.

In the context of factor analysis, selected strategy variables $R_{G\to S}^{Copm}$ are presented by *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* composites, generated from the relevant responses in the questionnaire. The derivation of these composites is described in Section 3.3 of Literature Review and Hypotheses Chapter.

For examination of the *Strategy – Performance* association with composite business policy variables, the next regression equation is used:

$$R_{S\to P}^{Comp} = \alpha + \beta_1 TSW + \beta_2 CM + \beta_3 HRI + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \beta_7 IND_2 + \\ + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \qquad [11]$$

where $R_{S\to P}^{Comp}$ is one of the dependent performance variables;

TSW – Traditional Social Welfare;

CM – Cost Minimisation;

HRI – Human Resource Investment.

Dependent performance variables $R_{S\to P}^{Comp}$ are the same as in the general *Strategy – Performance* hypothesis estimation, i.e. percentage of sales exported within the CIS, percentage of sales exported outside the CIS, capacity utilisation, increase in volume of production, as positive performance indicators, and percentage of wages paid in a non-monetarily form, percentage of sales bartered and bankruptcy threat, as negative performance indicators.

Increase in the volume of production and bankruptcy threats are binary performance variables and require logistic regression for analysis, performed with equation [12]:

$$LOGIT(R_{S\to P}^{Comp}) = \alpha + \beta_1 TSW + \beta_2 CM + \beta_3 HRI + \beta_4 PLE + \beta_5 SIZE + \beta_6 IND_1 + \\ + \beta_7 IND_2 + \beta_8 IND_3 + \beta_9 IND_4 + \beta_{10} IND_5 + \varepsilon \qquad [12]$$

4.7 CONCLUSION

This Chapter provides a detailed analysis of data, methodology and research design employed in the conduct of this study. Firstly, the Introduction Section considers the differences and fields of application for qualitative and quantitative research, justifying the choice of quantitative analysis techniques for testing of the hypothesised relationships in this thesis.

The hypothesised relationships for *Governance – Strategy* and *Strategy – Performance* are examined on the data from the ILO Labor Force Survey, held in Russia during the year 2000 (and sometimes backed up by 1999 comparisons). Data were collected by ILO professionals, together with local Goskomstat agents, from the firms giving useable responses in Moscow, Moscow Region, Nizhni Novgorod and Ivanovo. The comparison of the ILO sample with the official Goskomstat employment figures for the four selected regions allows to say that ILO distribution is very close to official industrial classification, with significant differences (at the 5% level) identified only for Metallurgy and Wood & Paper industries. This implies quite high industrial representativeness of the sample, although originally the ILO survey was not intended to be representative of either the whole country, or selected regions.

A variety of data, available from the ILO questionnaire, raised also the questions of appropriate statistical techniques and models for hypotheses testing. It is known that regression models must be correctly specified in terms of the proposed functional form and variables included in it. Thus, due to the presence of heteroskedasticity, confirmed by Breusch-Pagan tests, majority of regressions utilise Huber/White/sandwich modifications of OLS and LOGIT (chosen for continuous, categorical and binary variables) for testing of the stated eight hypotheses. Together with the models, this Chapter presented the Main Independent Variables (Subsection 4.3.1), Main Dependent Variables (4.3.2), Composite Strategic Variables (4.3.3) and Controls (4.3.4), constructed from questionnaire responses.

Following the preceding discussion in Chapter III on a choice of composite business strategy variables and their appropriateness for Russia (discussed in terms of the second

approach of this study), three relevant HRM strategic bundles were developed in this Chapter on the basis of these theoretical expectations. For this purpose, the three coherent HRM dimensions, representing correspondingly *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* HRM strategies of Russian enterprises, were constructed from relevant questionnaire responses. Section 5.5 below presents the results of explanatory cluster analysis, which was performed to justify the correct classification of these bundles. Also, some issues, associated with the limitations of cross-sectional data available for research, were discussed in this Chapter.

To answer the main research questions and to obtain the results, presented in the next Chapter, all descriptive and statistical analysis was performed with the help of Intercooled Stata 7.0 and SPSS 10.0 software.

CHAPTER V. Results and Statistical Inference

5.1 INTRODUCTION

This Chapter intends to provide answers to the main research questions of this study, addressed via eight testable hypotheses, focusing on *Governance – Strategy* and *Strategy – Performance* mechanisms, gradually introduced in Chapter III above, and informed by the relevant literature. The hypothesised associations between *governance* parameters and firm *strategies* are approached with such CG parameters, as ownership proportions held by company employees, and legal company forms. With the main interest of this research on employee welfare in Russian post-privatised industrial firms, the association between *strategies* and *performance* focuses on HRM strategies only.

The preceding examination of Western Strategic Management literature, concerned particularly with HRM issues, allowed us to develop and adopt three distinctive HRM strategies, suitable for Russian research. In particular, the identified strategies comprise *Traditional Social Welfare (TSW)*, *Cost Minimisation (CM)* and *Human Resource Investment (HRI)*.

Following the introduction of regression models and statistical techniques, applied to this research, this Chapter commences with Descriptive Statistics on parameters, used for the analysis (Section 5.2). These statistics give data on average earnings in sampled companies (see Table 7), and also present correlations between the variables used for hypothesis testing (see Table 8). In addition to Section 5.2, it is worth drawing the reader's attention to Tables 4-6 in Chapter IV, which presented data on property legal form distribution, industrial sector classification and shareholdings in companies of the considered ILO sample.

Section 5.3 presents the results of statistical testing of the main *Governance – Strategy* hypothesis. Subsequently, Section 5.4 presents the results for *Strategy – Performance* relationships hypothesised. The presentation of the results is accompanied by the relevant

discussion on the validity of these results, and their relevance. After that, Section 5.5 presents the results of tested associations between *Governance – Strategy* and *Strategy – Performance* with the three coherent bundles, representing *TSW*, *CM* and *HRI* strategies. However, to show that the conceptualised strategy bundles discriminate well between each other, results of the stepwise discriminant analysis (accompanied with ANOVA results) are first presented in Section 5.5.

To guide the reader though the findings, each section, presenting the results of hypothesis testing, ends with Tables that summarise the parameters, that suggest the acceptance or rejection of a particular hypothesis. Finally, Section 5.6 concludes with the summary of all the major findings of this Chapter.

5.2 DESCRIPTIVE STATISTICS

While a wide variety of model specifications were employed, this Chapter draws attention to the main results, reported in Tables 7 to 20. First, some descriptive statistics on average earnings (wages and bonuses) is given for the three groups of workers: managers, skilled and unskilled workers:

Table 7. Sample Average Earnings (in 000 Roubles, June 2000)

Property Form	Total Number of Employees	Managers	Skilled Workers	Unskilled Workers
Wages				
State Enterprise	2,074.11	3,453.98	1,991.84	1,025.38
Partnership	1,538.41	2,840.47	1,317.97	531.83
Closed Joint Stock Company	1,829.24	3,549.34	1,786.12	989.37
Open Joint Stock Company	1,861.84	3,642.61	1,861.14	960.22

Bonuses				
State Enterprise	625.65	1,001.13	602.78	286.29
Partnership	246.90	420.58	243.39	121.03
Closed Joint Stock Company	317.70	622.52	304.72	160.15
Open Joint Stock Company	504.33	950.54	503.69	244.37
Benefits as Percentage of Wages				
State Enterprise	21.35	19.53	24.53	7.49
Partnership	33.52	25.47	30.56	19.44
Closed Joint Stock Company	27.39	25.90	34.57	18.22
Open Joint Stock Company	42.88	24.73	65.76	14.73

From Table 7 above we can see that for combined enterprise property forms, wages and bonuses are about two times higher for managers than for skilled workers, whose earnings exceed those for the unskilled ones. Here, the largest difference occurs in wages in partnerships. For all three groups of employees, bonuses are higher in State enterprises, then come open JSCs, closed JSCs, and then partnerships. The same is true for wages with only two exceptions: for managers, wages are higher in JSCs than in State enterprises; the second is for unskilled workers, who earn more in closed JSCs than in open JSCs.

These results also show that, except for the JSCs, employees in State enterprises are generally better paid. The comparison of benefits provided in relation to wages, suggests that in State enterprises, benefits (as the percentage of wages paid) are smaller than in enterprises with other property forms – JSCs and partnerships. On the one hand, this result simply means that in partnerships and JSCs, benefits are generally higher than in the State companies. On the other hand, this finding could imply that the total yearly earnings of employees in the State enterprises (measured as wages plus all benefits provided) are more stable than in JSCs and partnerships once the variable part (i.e. benefits) of the total yearly income is smaller. So, this finding could have implications for the employees of all companies.

Descriptive statistics and pair-wise correlation coefficients for the variables included in the models are given the Table 8. Consistent with much prior research, most of the

coefficients in the correlation analysis have the predicted signs, high levels of significance, and provide reasonable support for hypothesised relations between *Governance – Strategy* and *Strategy – Performance*. Of course, more refined multiple regressions will be more relevant in this context.

Table 8. Descriptive Statistics and Correlation Matrix

	Variables	Mean	Std. Dev.	2	3	4	5	6	7
1	Managers' Shares	38.66	34.85	**-0.43****	**0.25****	0.13	**-0.26****	**-0.22****	**-0.24****
2	Workers' Shares	27.53	29.96		**-0.25****	**0.30****	-0.07	**0.26****	**0.28****
3	Partnership	0.13	0.33			**-0.20****	**-0.38****	**-0.16****	**-0.17****
4	Closed JSC	0.22	0.41				**-0.53****	-0.03	-0.02
5	Open JSC	0.51	0.50					**0.16****	**0.14***
6	Proportion of Benefits Received (Admin Workers)	0.41	0.17						**0.96****
7	Proportion of Benefits Received (Regular Workers)	0.42	0.18						
8	Wage Share of Production Costs	24.18	16.45						
9	Social Cost Share of Production Costs	7.23	17.57						
10	Training Share of Production Costs	0.38	1.21						
11	Labour Turnover (Total)	54.77	92.00						
12	Labour Turnover (Dismissed)	4.69	17.20						
13	Labour Turnover (Resigned)	34.86	57.52						
14	Remuneration System (Wage + Monthly Bonuses)	0.50	0.50						
15	Initial Training	0.74	0.44						
16	Training to Upgrade	0.66	0.47						
17	Increase in Training	0.26	0.44						
18	Retraining to Improve Job Performance	0.49	0.50						
19	Unpaid Leave	1.11	7.75						
20	% of Sales Exported Within the CIS	2.27	8.38						
21	% of Sales Exported Outside the CIS	2.64	11.25						
22	% of Sales Bartered	6.12	13.83						
23	Capacity Utilisation	60.22	27.71						
24	Increase in Volume of Production	0.57	0.50						
25	% of Wages Paid Non-monetarily (Workers)	33.97	21.91						
26	% of Wages Paid Non-monetarily (Engineers)	30.92	21.84						
27	Bankruptcy Threat	0.06	0.23						
28	Part of Larger Enterprise	0.08	0.27						
29	Ln Employment	5.49	1.34						

	8	9	10	11	12	13	14	15	16	17	18	19	20	21
1	**0.26****	-0.07	**-0.16†**	**-0.17***	-0.02	**-0.20***	**-0.20***	**-0.29****	**-0.33****	**-0.18***	-0.12	-0.03	0.02	-0.09
2	-0.11	**0.16†**	0.04	**0.18***	0.11	0.13	**0.24****	0.11	**0.17***	0.10	0.00	-0.09	0.06	0.07
3	0.00	**-0.10†**	-0.03	-0.03	-0.05	-0.03	**-0.18****	**-0.15****	**-0.23****	**-0.11†**	-0.07	-0.04	-0.09	0.01
4	-0.04	-0.02	0.07	-0.04	-0.03	0.00	**0.11†**	-0.03	-0.02	-0.04	0.01	-0.02	-0.01	-0.03
5	0.05	0.09	-0.01	0.07	0.08	0.05	0.03	**0.15***	**0.21****	**0.16****	**0.13***	0.08	0.05	0.03
6	0.01	**0.22****	**0.24****	**0.19****	**0.11†**	**0.17****	**0.27****	**0.32****	**0.43****	**0.17****	**0.32****	-0.04	**0.11†**	0.09
7	0.00	**0.23****	**0.24****	**0.20****	**0.12***	**0.19****	**0.27****	**0.34****	**0.45****	**0.20****	**0.29****	-0.07	**0.12***	0.07
8		-0.05	-0.01	-0.08	-0.05	-0.04	**-0.14***	-0.04	-0.04	0.00	0.04	0.02	-0.01	**0.11†**
9			0.06	**0.40****	**0.38****	**0.18****	0.04	**0.11†**	**0.13***	0.07	0.09	-0.02	0.06	0.03
10				**0.18****	**0.24****	**0.13***	0.03	**0.14***	**0.10†**	**0.17****	0.08	-0.01	**0.17****	**0.15****
11					**0.62****	**0.86****	**0.10†**	**0.16****	**0.17****	**0.16****	**0.13***	-0.01	**0.34****	**0.17****
12						**0.39****	0.00	0.08	0.09	0.05	0.09	-0.02	**0.25****	**0.20****
13							0.09	**0.13***	**0.15***	**0.15****	**0.10†**	-0.01	**0.39****	**0.14***
14								**0.19****	**0.32****	**0.17****	**0.14***	-0.07	-0.06	0.07
15									**0.63****	**0.32****	**0.39****	0.01	0.09	0.06
16										**0.33****	**0.39****	-0.03	0.08	0.06
17											**0.23****	0.05	-0.06	**0.13***
18												-0.03	0.09	0.01
19													-0.03	0.03
20														0.02
21														
22														
23														
24														
25														
26														
27														
28														
29														

	22	23	24	25	26	27	28	29
1	-0.07	0.02	**-0.20***	-0.10	-0.06	-0.06	0.12	**-0.23****
2	0.10	**0.20***	0.04	**0.18***	**0.20***	-0.01	-0.09	**0.28****
3	-0.08	**0.20****	-0.02	**-0.12***	**-0.12***	-0.09	**0.11†**	**-0.20****
4	-0.01	-0.06	0.08	0.07	0.07	-0.09	**-0.16****	0.02
5	**0.12***	**-0.11†**	0.04	0.04	0.07	0.04	-0.03	**0.20****
6	0.06	0.09	**0.15****	**0.27****	**0.32****	-0.07	0.00	**0.41****
7	0.07	**0.10†**	**0.18****	**0.26****	**0.29****	-0.08	0.03	**0.44****
8	-0.06	0.09	-0.06	-0.02	-0.08	-0.02	-0.05	**-0.12***
9	0.08	0.09	0.05	**0.18****	**0.12***	-0.03	0.04	**0.34****
10	0.08	0.03	0.07	**0.13***	**0.10†**	-0.07	-0.03	**0.19****
11	**0.12***	-0.02	0.05	**0.17****	**0.12***	-0.02	-0.02	**0.67****
12	**0.13***	-0.01	-0.05	**0.10†**	**0.10†**	-0.02	-0.03	**0.39****
13	0.09	-0.05	0.07	0.10†	0.06	-0.04	-0.02	**0.61****
14	**0.14***	-0.06	**0.14***	**0.34****	**0.39****	0.01	-0.08	**0.17****
15	**0.11†**	**0.11†**	**0.28****	**0.15****	0.07	-0.05	0.03	**0.30****
16	0.06	0.04	**0.28****	**0.23****	**0.24****	-0.04	0.00	**0.33****
17	**0.20****	0.01	**0.23****	**0.21****	**0.17****	0.02	-0.04	**0.17****
18	0.08	**0.11†**	**0.16****	**0.15***	**0.12***	**-0.13***	-0.07	**0.20****
19	0.08	**-0.16****	-0.06	0.02	-0.07	0.02	-0.04	-0.02
20	0.03	0.00	0.03	0.05	0.00	**0.11†**	-0.07	**0.27****
21	0.05	0.06	-0.02	**0.14***	**0.12***	-0.01	-0.04	**0.15****
22		-0.05	0.03	**0.10†**	0.03	0.03	**-0.10†**	**0.13***
23			0.04	0.02	-0.01	**-0.21****	0.07	-0.09
24				0.09	0.08	**-0.11†**	-0.06	**0.22****
25					**0.77****	0.03	-0.04	**0.29****
26						0.07	0.00	**0.26****
27							-0.02	-0.05
28								0.05
29								

† significant at 10% level; * significant at 5% level; ** significant at the 1% level

5.3 GOVERNANCE – STRATEGY RELATIONS

The preceding discussion on the results of privatisation in Russia and a subsequent *Governance – Strategy* review indicate that the Russian mass privatisation programme conveyed most property rights to managers and workers, as enterprise insiders. In terms of the proposed stakeholder approach, this outcome of privatisation raises the question of shareholder value distribution. In particular, are managers and workers likely to divert shareholder value towards their immediate sources of welfare (such as employment stability, wages, multiple social provisions) as employees, rather than as shareholders?

To answer this question, the first main *Governance – Strategy* hypothesis was developed in the context of this thesis. The results of tests on *Hypothesis 1* (stating that higher levels of workers' ownership will be positively associated with strategies that direct more resources towards immediate sources of employee welfare, e.g. higher wages, job preservation, social benefits etc.), are presented in Table 9.

Tests of *Hypothesis 1* are based on the two regression equations [1] and [2], described in the Section 4.6. The first three rows of the Table show the main association between insider ownership (workers', managers' and managers' squared) and employee welfare strategies, measured as continuous variables. Following the discussion in Chapter IV, the sample is restricted to those firms (with an average of 127 out of the 295 sampled for this study), where ownership may be expected to change, i.e. open and closed JSCs. This restriction was made deliberately, because managers and workers have significant equity stakes in closed and open JSCs (see Table 6 in Chapter IV), and this concentrated ownership may produce larger effects that with other, more dispersed ownership structures (Djankov and Murrell, 2002).

Table 9. Insider Equity and Firm Strategies (Robust Regression [White Estimator], OJSC and CJSC Only)

	Proportion of Total Range of Benefits Received (Administrative Workers)		Proportion of Total Range of Benefits Received (Regular Workers)		Wage Share of Production Costs, 1999		Labour Turnover (June 1999 – June 2000)					
							Total		Dismissed		Resigned	
Managers' Shares	-0.022	**0.253**	-0.049	**0.243**	0.041	0.063	3.045	-31.300	0.037	0.563	- 6.849	-17.098
	(-0.48)	**(1.75)†**	(-1.04)	**(1.61)†**	(1.02)	(0.51)	(0.18)	(-0.57)	(0.08)	(0.38)	(-0.66)	(-0.63)
Managers' Shares Squared		**-0.003**		**-0.004**		-0.001		0.366		-0.006		0.109
		(-2.04)*		**(-2.17)***		(-0.20)		(0.66)		(-0.37)		(0.44)
Workers' Shares	**0.102**	**0.095**	**0.107**	**0.108**	0.066	0.065	13.389	13.956	-0.051	-0.078	-5.403	-5.234
	(1.92)†	**(1.94)†**	**(2.19)***	**(2.07)***	(1.60)	(1.56)	(0.58)	(0.59)	(-0.11)	(-0.16)	(-0.49)	(-0.47)
Controls:												
Part of Larger Enterprise	0.070	0.075	**0.109**	**0.114**	0.029	0.026	-16.232	-16.852	-0.517	-0.540	0.234	0.049
	(1.05)	(1.12)	**(1.64)†**	**(1.74)†**	(0.54)	(0.54)	(-0.95)	(-0.92)	(-0.85)	(-0.85)	(0.02)	(0.00)
Ln Employment	0.020	0.014	0.019	0.012	**-0.035**	**-0.035**	**47.613**	**48.343**	**0.427**	**0.441**	**22.107**	**22.325**
	(1.28)	(0.87)	(1.20)	(0.77)	**(-3.33)****	**(-3.27)****	**(4.79)****	**(4.75)****	**(3.47)****	**(3.45)****	**(4.51)****	**(4.58)****
Food	**0.119**	**0.111**	**0.088**	**0.079**	**-0.084**	**-0.084**	-19.482	-18.532	-0.433	-0.466	**-12.865**	**-12.581**
	(2.93)**	**(2.77)****	**(2.08)***	**(1.89)***	**(-2.58)****	**(-2.57)****	(-1.53)	(-1.39)	(-1.15)	(-1.18)	**(-1.95)***	**(-1.87)†**
Light	**0.061**	**0.056**	0.053	0.048	-0.021	-0.022	11.785	12.350	0.025	0.009	5.845	6.015
	(1.74)†	**(1.68)†**	(1.51)	(1.44)	(-0.75)	(-0.76)	(0.57)	(0.59)	(0.08)	(0.03)	(0.64)	(0.65)
Wood & Paper	**0.115**	0.102	0.078	0.064	-0.015	-0.017	**-37.724**	**-36.072**	0.066	-0.009	**-21.076**	**-20.583**
	(1.76)†	(1.59)	(1.24)	(1.05)	(-0.26)	(-0.29)	**(-2.12)***	**(-1.98)***	(0.10)	(-0.01)	**(-2.53)***	**(-2.25)***
Chemistry	0.037	0.032	0.035	0.029	-0.023	-0.023	7.368	7.901	-0.241	-0.286	10.828	11.017
	(0.83)	(0.66)	(0.74)	(0.58)	(-0.59)	(-0.60)	(0.66)	(0.70)	(-0.54)	(-0.61)	(1.35)	(1.37)
Construction Materials	-0.066	-0.083	-0.055	-0.073	-0.015	-0.017	-12.146	-10.053	0.378	0.332	- 9.203	-8.578
	(-1.33)	(-1.54)	(-1.19)	(-1.44)	(-0.34)	(-0.37)	(-0.69)	(-0.54)	(0.72)	(0.60)	(-0.81)	(-0.73)
Constant	**0.262**	**0.270**	**0.294**	**0.303**	**0.040**	**0.040**	**-22.465**	**-22.490**	**-1.515**	**-1.594**	**-88.572**	**-88.878**
	(2.90)**	**(2.99)****	**(3.18)****	**(3.27)****	**(5.77)****	**(5.75)****	**(-3.59)****	**(-3.58)****	**(-1.85)***	**(-1.91)†**	**(-3.39)****	**(-3.40)****
Observations	128	128	128	128	126	126	128	128	127	128	128	128
R-squared	0.18	0.21	0.17	0.19	0.13	0.11	0.45	0.45	0.18	0.18	0.40	0.40
F-statistics (Prob>F)	3.26	3.41	3.33	3.52	2.15	1.93	3.97	3.68	2.16	2.11	5.88	5.31
	(0.001)	(0.001)	(0.001)	(0.000)	(0.031)	(0.050)	(0.000)	(0.000)	(0.030)	(0.029)	(0.000)	(0.000)

Robust t-statistics in parentheses; † significant at 10% level; * significant at 5% level; ** significant at the 1% level

The proportion of the total range of benefits[5] provided for administrative and regular workers shows a significant association with linear representations of both workers' and managers' ownership. However, only four coefficients are significant (5% level) and have interpreted signs (with two coefficients close to zero). In particular, workers' shareholdings are positively and significantly (at the 5% level) associated with the proportion of the total range of benefits received by regular workers. This may be interpreted as follows: if MO and all other controls in the regression are held constant, a one unit change in WO is associated with a 0.108 increase in the proportion of benefits provided to regular workers. This relation may indicate that workers, acting as shareholders, have a consistent influence on HRM strategies that immediately favour employees and are likely to transfer any achieved surplus of the enterprise into a form of benefits.

Columns (1) and (3) of Table 9 show no significant association between managerial ownership (MO) and any variable relating to employee welfare. However, to address possible non-linearities, and following Morck *et al.* (1988), a quadratic term on managerial ownership (MO^2) was included. In this case, MO continues to be insignificant (10% level), but the quadratic term is significant (5% level) and negative. As with the interpretation of WO, if MO, WO and the controls are held constant, a one unit change in MO^2 will cause a decrease in benefits to workers by 0.004 units (0.003 for administrative workers, both significant at the 5% level). Being inconsistent with *Hypothesis 1*, this result suggests provisionally that MO may be associated with benefits for employees exponentially, first going up with increasing MO and then falling down after MO passes some threshold level. Perhaps with MO at low levels, managers feel obliged to collude with workers in the provision of benefits to employees, but feel able to challenge them at higher levels. Nevertheless, it must be conceded that the coefficients are close to zero, and thus the possible degree of "exploitation" of workers seems negligible.

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[5] The variable for the proportion of total benefits received was constructed from the listed benefits, ranged from paid vacation, additional vacation, rest houses, sickness benefit, paid health services, subsidised rent, subsidised kindergartens and bonuses to profit sharing, loans, retiring assistance, supplementary pension, subsidy for canteen or benefit for meal, subsidised consumer goods, transport subsidies and unpaid shares (see Questions 34-35 in Appendix I for a full list of benefits provided).

Other results provide no significant association between the described ownership forms and labour turnover variables or wage share of production. It is interesting to note that labour dismissals, for example, are not significantly associated with either workers' or managers' ownership, whereas numerous layoffs have been reported for most of Russian "employee-owned manager-controlled" (Earle and Estrin, 1996) manufacturing firms. At the same time, the result for wages as a share of production costs may imply that either workers (in their role as shareholders) do not have control over wage flows, or managers do not provide workers with low payments, or delay them. From these points of view, enterprise retrenchment has to be explained in terms of business crisis and non-governance variables (Buck *et al.*, 1999), rather than ownership proportions.

To hold the non-hypothesised influences constant, a number of control variables were included into the regressions. The use of the establishment size, measured as the logarithm of absolute number employed, was supported by a number of significant coefficients obtained. In particular, significant and positive signs on the size control variable indicate that in larger firms of the considered sample, labour turnover is also generally higher. Also size of the enterprise has a negative and highly significant (at the 1% level) association with wage share of production costs. This may be interpreted as indicating the unwillingness (or inability) of large firms that dominate local labour markets to allocate substantial funds for wages.

Besides the establishment size, "part of the larger enterprise" and five industrial sector controls were introduced. While the first control parameter does not indicate any significant difference between independent enterprises and those that are parts of the larger ones, results for industry controls vary a lot across Table 9. Among them, the Food industry is the one that exhibits the highest number of significant coefficients.

Following the results of *Hypothesis 1* testing for continuous variables, Table 10 presents the results of analysis of the same hypothesis, but for binary *strategy* variables. This analysis is based on logistic regression equations [4] and [5]. Binary variables include the "remuneration system in the form of basic wage with monthly bonuses", "initial training", "training to upgrade", "increase in training" and "retraining to improve job performance".

Of five significant (at the 5% level or better) coefficients for *Governance – Strategy* elements, two are of the hypothesised sign, and three oppose *Hypothesis 1*. For example, higher managerial ownership has a negative and significant impact on training to upgrade (at the 1% level) and increase in training (at the 1% level), which implies that managers, as relational shareholders, are not likely to encourage and subsidise any form of training as an HRM *strategy*, favouring employee welfare. Besides, negative signs for retraining to improve job performance, and initial form of training, indicate that these forms of training may also be opposed by managers, since these associations are either insignificant or present a low (the 10%) level of significance. In addition, there is no significant association between workers' ownership and the four described forms of training. Thus, one may speculate that the question of training does not loom large in the preferences of workers, and being shareholders does not obviously influence their strategic decisions. Nonetheless, the negative and significant result for managers contradicts *Hypothesis 1* in terms of training as a welfare parameter, and leads to its rejection.

One more significant result for binary *strategy* variables relates to workers' shareholdings in relation to the remuneration system. Here, workers' ownership shows a significant (at the 5% level) and positive association with a remuneration system comprising basic wages and monthly bonuses. This finding could be interpreted, as with the association between workers' ownership and the provision of benefits (see Table 9), workers may also have a consistent influence on the remuneration strategies of their enterprises.

The introduction of a quadratic term of managerial ownership for binary strategy variables, suggested by Morck *et al.* (1988), gave however no improvement in terms of total fit. The coefficient for MO^2 is negative and significant (at the 5% level) in relation to training to upgrade only. The fact that this coefficient is negative can be treated as opposed to *Hypothesis 1*, implying that managers do not support this form of training. The use of various controls in the regressions did not lead to any consistently significant results, except those described above for continuous variables.

Table 10. Insider Equity and Firm Strategies (LOGIT, OJSC and CJSC Only)

	Remuneration System Basic Wage with Monthly Bonuses		Initial Training		Training to Upgrade		Increase in Training		Retraining to Improve Job Performance	
Managers' Shares	0.132	0.496	**-1.424**	1.545	**-2.113**	2.058	**-1.976**	1.824	-0.646	-1.478
	(0.19)	(0.22)	**(-1.75)†**	(0.62)	**(-2.51)****	(0.87)	**(-2.51)****	(0.69)	(-0.94)	(-0.69)
Managers' Shares Squared		-0.004		-0.031		**-0.044**		-0.045		-0.009
		(-0.17)		(-1.26)		**(-1.96)***		(-1.36)		(-0.41)
Workers' Shares	**1.684**	**1.674**	0.116	-0.015	-0.350	-0.428	-0.180	-0.159	-0.224	-0.210
	(2.25)*	**(2.24)***	(0.12)	(-0.02)	(-0.41)	(-0.53)	(-0.23)	(-0.21)	(-0.31)	(-0.29)
Controls:										
Part of Larger Enterprise	**-2.308**	-2.322	0.879	1.049	**1.348**	**1.587**	-0.115	0.243	0.538	0.514
	(-1.96)*	(-1.98)	(0.79)	(0.88)	**(1.75)†**	**(1.79)†**	(-0.08)	(0.16)	(0.62)	(0.60)
Ln Employment	0.068	0.060	**0.371**	0.310	0.117	0.022	0.006	-0.073	0.234	0.253
	(0.35)	(0.30)	**(1.70)†**	(1.44)	(0.59)	(0.10)	(0.03)	(-0.35)	(1.23)	(1.29)
Food	**1.681**	**1.674**	0.353	0.284	-0.087	-0.189	**-2.765**	**-2.865**	**1.311**	**1.336**
	(2.46)**	**(2.44)***	(0.49)	(0.38)	(-0.14)	(-0.30)	**(-2.60)****	**(-2.68)****	**(2.18)***	**(2.16)***
Light	**1.078**	**1.071**	**1.221**	**1.188**	0.220	0.154	0.025	-0.011	**1.374**	**1.389**
	(2.20)*	**(2.18)***	**(2.02)***	**(1.96)***	(0.42)	(0.29)	(0.05)	(-0.02)	**(2.75)****	**(2.77)****
Wood & Paper	-0.621	-0.636	-0.838	-0.941	0.382	0.178	-1.121	-1.282	0.035	0.073
	(-0.62)	(-0.64)	(-0.87)	(-0.97)	(0.31)	(0.15)	(-0.93)	(-1.06)	(0.04)	(0.08)
Chemistry	0.029	0.022	-0.087	-0.149	0.301	0.233	-0.627	-0.710	-0.082	-0.068
	(0.05)	(0.03)	(-0.11)	(-0.19)	(0.39)	(0.27)	(-0.79)	(-0.85)	(-0.12)	(-0.10)
Construction Materials	0.674	0.646	-0.255	-0.459	0.503	0.217	0.464	0.262	0.718	0.772
	(0.90)	(0.85)	(-0.30)	(-0.53)	(0.53)	(0.23)	(0.61)	(0.34)	(0.98)	(1.04)
Constant	-1.188	-1.174	-0.598	-0.527	1.071	1.200	0.241	0.333	-1.504	-1.535
	(-0.93)	(-0.92)	(-0.41)	(-0.37)	(0.74)	(0.84)	(0.19)	(0.26)	(-1.21)	(-1.22)
Observations	128	128	128	128	128	128	128	128	128	128
Pseudo R-squared	0.11	0.11	0.11	0.12	0.10	0.12	0.14	0.15	0.09	0.09
Wald Chi-square (Prob>Chi-square)	18.34	18.21	19.49	19.41	14.74	15.10	15.47	15.21	14.56	14.80
	(0.048)	(0.051)	(0.038)	(0.041)	(0.104)	(0.091)	(0.087)	(0.096)	(0.097)	(0.101)

Robust Z-statistics in parentheses; † significant at 10% level; * significant at 5% level; ** significant at the 1% level

Tables 11 and 12 provide the results of *Governance – Strategy* hypothesis testing with continuous *governance* (insider ownership) variables replaced with legal forms of enterprises, including open JSCs, closed JSCs and partnerships, presented in the form of dummies. In this context, open JSCs for example, may be expected to attract more resources from outside capital markets, and thus offer higher levels of employee benefits. For these tests, dependent, continuous *strategy* variables include, as before, the proportion of the total range of benefits provided for administrative and regular workers, wage, training and social cost shares of production costs; and also "layoffs", "remuneration system in the form of basic wage with monthly bonuses", "initial training", "training to upgrade", "increase in training" and "retraining to improve job performance" for binary *strategy* variables.

However, the results of regression [3] analysis provide no support for this supposition, as legal form of the enterprise has no significant association with proportions of benefits received, wage, training and social cost shares of production costs.

Enterprise size, measured by the logarithm of the total number employed, has highly significant signs, showing that large enterprises slightly outperform the small ones, except in terms of wage share of production costs. This variable, as in the analysis for different ownership structures (Table 9), is negative and fairly significantly associated with the size control.

Table 11. Legal Forms and Firm Strategies (Robust Regression [White Estimator])

	Proportion of Total Range of Benefits Received (Administrative Workers)	Proportion of Total Range of Benefits Received (Regular Workers)	Wage Share of Production Costs, 1999	Social Cost Share of Production Costs, 1999	Training Share of Production Costs, 1999
Legal Forms:					
Partnership	-0.041	**-0.063**	0.018	-0.028	0.002
	(-1,17)	**(-1,76)†**	(0,48)	(-0,73)	(0,46)
Closed JSC	-0.017	-0.028	0.008	-0.017	0.002
	(-0,55)	(-0,89)	(0,25)	(-0,50)	(0,83)
Open JSC	0.014	-0.004	0.033	0.001	0.001
	(0,51)	(-0,13)	(1,15)	(0,01)	(0,07)
Controls:					
Part of Larger Enterprise	0.001	0.017	-0.031	0.019	-0.002
	(0,02)	(0,49)	(-0,88)	(0,51)	(-0,58)
Ln Employment	**0.054**	**0.058**	**-0.020**	**0.042**	**0.0018**
	(7,30)**	**(7,79)****	**(-2,52)****	**(5,28)****	**(3,13)****
Food	**0.081**	**0.063**	**-0.105**	-0.021	0.001
	(2,89)**	**(2,21)***	**(-3,57)****	(-0,69)	(0,31)
Light	0.022	0.018	**-0.049**	0.018	-0.001
	(0,92)	(0,75)	**(-1,89)†**	(0,69)	(-0,60)
Wood & Paper	**0.088**	**0.074**	-0.045	0.035	**0.006**
	(2,22)*	**(1,84)†**	(-1,08)	(0,83)	**(2,10)***
Chemistry	0.046	0.056	-0.035	-0.002	0.002
	(1,30)	(1,57)	(-0,94)	(-0,05)	(0,60)
Construction Materials	-0.057	-0.043	-0.037	-0.050	0.002
	(-1,52)	(-1,14)	(-0,97)	(-1,25)	(0,74)
Constant	**0.092**	**0.092**	**0.368**	**-0.153**	**-0.007**
	(1,99)*	**(1,96)***	**(7,54)****	**(-3,06)****	**(-1,97)***
Observations	295	295	286	291	293
R-squared	0.23	0.23	0.07	0.13	0.06
F-statistics (Prob>F)	8.02	9.39	2.20	2.78	1.90
	(0.000)	(0.000)	(0.018)	(0.003)	(0.045)

Robust t-statistics in parentheses

† significant at 10% level; * significant at 5% level; ** significant at the 1% level

For binary variables (Table 12 and regression [6]), legal forms of the enterprise are mostly insignificant as well, except for the partnership dummy which has a significant (at the 5% level) and negative association with training to upgrade and a significant (at the 1% level) and negative association with the presence of a remuneration system with basic wages and monthly bonuses. This negative association for the partnership legal form may imply that share-owning managers in partnerships resist demands for employee-favouring benefits.

As before, size of the enterprises is important for benefits offered, as positive and highly significant coefficients suggest.

Table 12. Legal Forms and Firm Strategies (LOGIT)

	Layoffs	Remuneration System Basic Wage with Monthly Bonuses	Initial Training	Training to Upgrade	Increase in Training	Retraining to Improve Job Performance
Legal Forms:						
Partnership	0.496	**-1.293**	-0.725	**-1.014**	-0.330	0.294
	(1.02)	**(-2.49)****	(-1.42)	**(-2.07)***	(-0.49)	(0.64)
Closed JSC	**0.786**	0.122	-0.350	-0.185	0.130	0.428
	(1.80)†	(0.28)	(-0.76)	(-0.41)	(0.25)	(1.01)
Open JSC	0.405	-0.352	0.072	0.338	0.664	**0.645**
	(1.05)	(-0.95)	(0.18)	(0.88)	(1.41)	**(1.74)†**
Controls:						
Part of Larger Enterprise	0.029	-0.433	0.300	0.048	-0.354	-0.501
	(0.06)	(-0.81)	(0.49)	(0.09)	(-0.63)	(-1.04)
Ln Employment	**0.295**	**0.325**	**0.578**	**0.576**	**0.245**	**0.313**
	(2.96)**	**(3.04)****	**(4.42)****	**(4.66)****	**(2.30)***	**(3.03)****
Food	-0.200	**1.535**	0.611	0.260	**-1.056**	**0.607**
	(-0.51)	**(3.87)****	(1.27)	(0.62)	**(-1.91)†**	**(1.61)†**
Light	0.202	**0.921**	**0.696**	0.405	0.189	**0.514**
	(0.64)	**(2.74)****	**(1.81)†**	(1.07)	(0.54)	**(1.61)†**
Wood & Paper	0.460	-0.221	0.370	0.442	-0.035	0.249
	(0.84)	(-0.41)	(0.61)	(0.76)	(-0.07)	(0.48)
Chemistry	0.321	0.301	0.638	**0.855**	0.262	0.042
	(0.69)	(0.65)	(1.10)	**(1.64)†**	(0.48)	(0.09)
Construction Materials	-0.623	**0.861**	0.273	0.629	0.235	0.349
	(-1.18)	**(1.80)†**	(0.46)	(1.07)	(0.45)	(0.74)
Constant	**-2.377**	**-1.971**	**-2.216**	**-2.685**	**-2.700**	**-2.438**
	(-3.84)**	**(-3.02)****	**(-3.01)****	**(-3.77)****	**(-3.79)****	**(-3.77)****
Observations	295	295	295	295	295	295
Pseudo R-squared	0.05	0.10	0.10	0.13	0.07	0.06
Wald Chi-square (Prob>Chi-square)	18.98	33.65	28.63	44.37	16.75	19.36
	(0.041)	(0.000)	(0.001)	(0.000)	(0.080)	(0.036)

Robust Z-statistics in parentheses

† significant at 10% level; * significant at 5% level; ** significant at the 1% level

The following table summarises all the results for *Hypothesis 1* testing on *Governance – Strategy* relationship for different *governance* variables (share ownership and legal forms) and individual benefits provided.

Table 13. Summary, Hypothesis 1 Test Results (Tables 9-12)

	Supported for One Indicator	Rejected for One Indicator
For Different Ownership Structures (Tables 9, 10)		
Proportion of Total Range of Benefits Received (Administrative Workers)		√
Proportion of Total Range of Benefits Received (Regular Workers)	√	√
Remuneration System (Wage + Bonuses)	√	
Training to Upgrade		√√
Increase in Training		√
For Different Legal Forms (Tables 11, 12)		
Remuneration System (Wage + Bonuses)		√
Training to Upgrade		√

Hypothesis 1 states that higher levels of workers' ownership are positively associated with strategies that direct more resources towards immediate sources of employee welfare (e.g. higher wages, job preservation, social benefits, etc). The results, summarised in Table 13, are very mixed (with many insignificant results not presented, of course), but generally tend to refute *Hypothesis 1*, rather than support it.

This mixed result could be explained by the nature of cross-sectional data that may be insufficient to produce consistent patterns of *Governance – Strategy* results within one year. Another reason could be the choice of available *governance* variables from the ILO questionnaire. Finally, benefits given to employees may interact and the significance of benefits variables may only become apparent when they are clustered into the specific composite bundles, suggested by theory in Section 3.3, and empirically tested in Section 5.5 below.

Also, it has to be remembered that some ambiguity in the results, reported in Table 13, reflects (to certain extent) the nature and the results of the Russian privatisation programme. It was pointed out that Russian privatisation conveyed most property rights to enterprise insiders – managers and workers (Boycko *et al.*, 1995), arguably being more politically, than economically driven (Uhlenbruck and De Castro, 1998). Besides, a long tradition of benefit provision in the FSU, where substantial amounts of enterprise-level welfare provision (housing, kindergartens, polyclinics, etc.) were backed up by considerable State support (subsidised household materials and services, minimum wage legislation, etc.) has to be remembered too. Thus, the resulting shareholdings of Russian employees may be more likely to be diverted to reflect their perceptions and current wellbeing as employees, rather than as shareholders.

Disregarding all insignificant results, we can see that proportions of the benefits provided are controlled by the firm's insiders, particularly by workers. This association is significant and shows some improvement in the *governance* in Russian enterprises, where workers, acting as shareholders, have consistent influence on HRM strategies. In particular, this could imply that workers impose discipline on managers to choose strategies that immediately favour employees, thus this association can be taken as supportive for *Hypothesis 1*. Other findings suggest that various legal forms of the enterprises (partnership, open JSC or closed JSC) have no significant association with proportions of benefits received. This result follows Stark (2001), who warns that different property forms may act as a cosmetic device in Russia, and have a neutral effect, since they are built on the existing "Soviet" competences or routines (Spenner *et al.*, 1998). These "Soviet" routines of welfare provision represent a *status quo*, which is argued to be supported by company insiders and which may result in improved performance, and will be empirically examined later in this thesis via a cluster approach (under different hypotheses formulated, see Section 5.5).

The presence of a remuneration system in the form of wages with monthly bonuses was found to be positively associated with WO in relation to workers' pay only (Table 10). This result could be interpreted in the way that workers have a consistent influence on remuneration strategies of their enterprises, and managers do not seem to seriously oppose these strategies of workers. However, this form of welfare provision is not relevant to the

considered legal forms of enterprises, and is significantly and negatively associated with the partnership form only (Table 12).

Although it is recognised that most successful companies (in the US or the UK) put an emphasis on training and relevant training-focused activities (Pfeffer and Veiga, 1999), no form of training was found to be significant among the strategies that direct resources towards employee welfare, either for different ownership structures or for different legal forms of the enterprise. Here, managerial ownership in the enterprises was found to be negatively associated with spending on training, while for workers, this issue seemed to be outside their competences and influences, so that at least no significant association between workers' ownership and different forms of training was found. But, as noted, the result for managerial ownership suggests that they are not likely to train their employees and invest in intellectual human capital. This result could also imply that most of the employees considered in the ILO sample of manufacturing firms, have low productivity or have skills that are not in demand (Brown, 1998). Although this result is not repeated in relation to labour dismissals, non-provision of training to employees may represent one of managers' retrenchment strategies, in the short run at least.

5.4 STRATEGY – PERFORMANCE RELATIONS

After presenting the results on *Governance – Strategy* tests, this Section continues to examine the outcomes of the Russian privatisation programme for *Strategy – Performance* relationships, with the aim of answering the question whether firms' strategic decisions, possibly directed to some extent at short-term employee welfare, are associated with stronger or weaker enterprise performance?

To answer this question, the second main *Strategy – Performance* hypothesis was developed in the context of this thesis. In particular, *Hypothesis 2* states that the firm's individual high-commitment strategies, promoting the welfare for the employees, will be positively associated with improved corporate performance. (By implication, individual

strategies that damage employee welfare, like layoffs, are predicted to be negatively associated with performance.)

Table 14 presents the results of regressions that test *Hypothesis 2*. For this test, the full sample is used and the analysis is based on regression [7] and logistic equation [8]. Following the discussion of appropriate *performance* indicators for Russia (see Subsection 4.3.2), where we noted that the use of stock market performance indicators or national accounting measures and ratios could lead to unreliable results (Hoskisson *et al.*, 2000), two sets of performance variables, representing: (a) *positive* performance indicators, i.e. the "percentage of sales exported within the CIS", the "percentage of sales exported outside the CIS", "capacity utilisation" and the "increase in volume of production"; and (b) *negative* performance indicators, i.e. the "percentage of wages paid non-monetarily", the "percentage of sales bartered" and the perceived "bankruptcy threat", were introduced. The choice of export variables, as dimensions of performance, is supported by Earle *et al.* (1996) and Filatotchev *et al.* (2001b); Driver and Thompson (2002) use the capacity utilisation rate in examining downsizing strategies. However, the use of negative performance indicators such as the "bankruptcy threat" or non-cash sales is claimed to be a novel aspect of this thesis.

Table 14 provides some support to the argument that *strategies* that promote (damage) employee welfare will be positively (negatively) associated with corporate *performance*. Of ten significant (at the 5% level or better) coefficients for *Strategy – Performance* elements, six are of the hypothesised sign, and four oppose *Hypothesis 2*. Also four weakly significant (at the 10% level) coefficients, that have the hypothesised sign, are left aside due to the low significance level.

It can be seen that higher wages, as a proportion of production costs, are positively and significantly (at the 5% level) associated with a higher percentage of sales exported outside the CIS, in the short term at least. However the same result does not occur for enterprises in relation to exporting within the CIS. This implies that firms exporting on domestic (i.e. CIS) markets are more wage-constrained in comparison with outside exporters. Outside exporters are also likely to increase training provision to its employees (though this association is weakly significant), whereas for the CIS exporters, this

association is significantly negative (at the 1% level). The last result is somewhat controversial, as enterprises exporting within the CIS already reported a significantly high level (at the 5% level) of training's share of production costs. Of course, one of the associations could be mechanical.

Some support for the efficacy of high commitment strategies is provided by other positive performance indicators – capacity utilisation rate and increase in the volume of production. The results suggest that the higher is the capacity utilisation rate, the greater is the spending on initial training (5% significance), and the lower is a number of workers on unpaid leave (significant at the 1% level, a negative strategy). Increases in the volume of production are again negatively and significantly (at the 5% level) associated with layoffs. Though again this could be a mechanical association, the discussion after the Summary Table 15 in this Section provides an alternative explanation of this negative association.

Positive and significant (at the 5% level) relationships between the capacity utilisation rate and the initial form of training for the employees may indicate a rise in the demand for a qualified work force in expanding or emerging enterprises. This latter interpretation is also supported by an increase in training provided associated with a 5% significant increase in the volume of production.

Table 14. Strategies and Firm Performance (Robust Regression; LOGIT where indicated)

	Positive Performance Indicators				Negative Performance Indicators			
	% of Sales Exported Within the CIS, 1999	% of Sales Exported Outside the CIS, 1999	Capacity Utilisation, 2000	Increase in Volume of Production (LOGIT)	% of Wages Paid Non-monetarily /Workers, 2000	% of Wages Paid Non-monetarily /Engineers 2000	% of Sales Bartered, 1999	Bankruptcy Threat (LOGIT)
Wage Share of Production Costs	-0.004	**0.091**	14.214	-0.006	0.039	-0.065	-0.061	-1.785
	(-0.15)	**(2.27)***	(1.45)	(-0.01)	(0.50)	(-0.85)	(-1.19)	(-1.10)
Social Cost Share of Production Costs	-0.042	-0.059	**17.328**	0.279	0.108	0.014	0.022	0.196
	(-1.39)	(-1.46)	**(1.74)†**	(0.24)	(1.37)	(0.18)	(0.42)	(0.13)
Training Share of Production Costs	**0.941**	0.332	8.564	16.515	1.077	0.223	0.278	-4.007
	(2.15)*	(0.57)	(0.06)	(1.05)	(0.95)	(0.20)	(0.37)	(-1.40)
Average Benefits for Administrative Workers	-0.051	0.137	1.779	**-5.728**	0.285	**0.701**	0.055	2.423
	(-0.54)	(1.07)	(0.06)	**(-1.97)***	(1.15)	**(2.87)****	(0.34)	(0.58)
Average Benefits for Regular Workers	0.055	-0.149	27.301	**4.479**	-0.188	**-0.483**	-0.014	-3.315
	(0.58)	(-1.17)	(0.88)	**(1.63)†**	(-0.76)	**(-2.00)***	(-0.09)	(-0.92)
Initial Training	0.007	-0.001	**9.900**	0.579	-0.035	**-0.097**	0.027	-0.151
	(0.50)	(-0.04)	**(2.04)***	(1.51)	(-0.94)	**(-2.63)****	(1.11)	(-0.19)
Training to Upgrade	0.005	-0.002	-6.466	**0.683**	**0.059**	**0.090**	-0.033	0.027
	(0.34)	(-0.10)	(-1.37)	**(1.86)†**	**(1.62)†**	**(2.51)****	(-1.39)	(0.03)
Increase in Training	**-0.030**	**0.030**	0.230	**0.759**	**0.066**	**0.063**	**0.049**	0.439
	(-2.50)**	**(1.87)†**	(0.06)	**(2.13)***	**(2.12)***	**(2.08)***	**(2.44)***	(0.71)
Unpaid Leave	-0.001	0.001	**-0.605**	-0.021	0.002	-0.002	0.001	0.014
	(-0.13)	(0.14)	**(-3.00)****	(-0.86)	(0.15)	(-1.25)	(1.10)	(0.98)
Layoffs	**0.001**	**0.001**	0.041	**-0.041**	-0.001	0.0001	0.001	0.020
	(2.35)*	**(2.60)****	(0.39)	**(-2.20)***	(-0.62)	(0.14)	(1.13)	(0.53)

Controls:								
Ln Employment	**0.013**	**0.011**	**-4.872**	**0.430**	**0.038**	**0.029**	0.008	0.042
	(2.88)**	**(1.72)†**	**(-3.21)****	**(2.77)****	**(3.16)****	**(2.48)****	(0.98)	(0.14)
Part of Larger Enterprise	-0.027	-0.008	6.644	-0.697	-0.029	0.008	**-0.054**	-0.163
	(-1.56)	(-0.34)	(1.15)	(-1.26)	(-0.64)	(0.18)	**(-1.81)†**	(-0.14)
Foreign Investment in Enterprise	**-0.090**	0.054	11.025	0.058	-0.089	-0.029	-0.094	-0.123
	(-1.84)†	(0.83)	(0.69)	(0.06)	(-0.71)	(-0.24)	(-1.13)	(-0.18)
Food	**-0.034**	-0.003	-0.179	**1.163**	**0.064**	0.046	-0.024	-1.103
	(-2.22)*	(0.00)	(-0.04)	**(2.74)****	**(1.61)†**	(1.19)	(-0.91)	(-0.95)
Light	**-0.021**	0.014	**13.474**	0.590	0.029	0.005	0.007	-0.069
	(-1.64)†	(0.80)	**(3.20)****	(1.52)	(0.89)	(0.15)	(0.32)	(-0.09)
Wood & Paper	-0.019	**0.128**	1.807	0.320	0.007	-0.016	-0.017	0.076
	(-0.90)	**(4.58)****	(0.26)	(0.55)	(0.12)	(-0.29)	(-0.47)	(0.06)
Chemistry	-0.012	**0.042**	-2.715	0.419	0.032	0.023	0.037	**1.278**
	(-0.65)	**(1.70)†**	(-0.45)	(0.79)	(0.66)	(0.50)	(1.26)	**(1.63)†**
Construction Materials	-0.031	-0.015	4.036	-0.538	-0.009	0.014	0.061	-0.223
	(-1.51)	(-0.56)	(0.62)	(-1.04)	(-0.18)	(0.28)	(1.80)	(-0.19)
Constant	-0.037	**-0.070**	**63.523**	**-2.812**	0.033	0.069	0.001	-1.939
	(-1.39)	**(-1.95)***	**(7.23)****	**(-3.18)****	(0.49)	(1.01)	(0.01)	(-1.33)
Observations	284	284	281	285	284	284	284	282
R^2 [LOGIT: PseudoR^2]	0.17	0.17	0.15	0.16	0.16	0.18	0.11	0.11
F-statistics (Prob>F) [LOGIT: Wald Chi-square (Prob>Chi-square)]	2.92	3.08	2.59	43.55	2.78	3.15	1.78	21.18
	(0.000)	(0.000)	(0.000)	(0.001)	(0.000)	(0.000)	(0.028)	(0.182)

Robust t-statistics (Robust Z-statistics for LOGIT) in parentheses

† significant at 10% level; * significant at 5% level; ** significant at the 1% level

The evidence in favour of *Hypothesis 2* in relation to negative performance indicators however, is more contradictory. Of seven significant coefficients, only two (in relation to wages paid non-monetarily to engineers) were of the hypothesised sign, and even for this negative performance measure, three other significant coefficients had the wrong sign (for average benefits, training to upgrade and increases in training). In total, five *strategy* coefficients for negative *performance* indicators had the wrong sign in relation to *Hypothesis 2*. On the one hand, these results for negative performance indicators are rather disappointing, as they mostly oppose *Hypothesis 2*, but on the other hand, they could be interpreted differently for the Russian post-privatisation environment.

In particular, it has to be remembered that after the mass privatisation programme, most Russian enterprises found themselves in a "business turnaround" situation, with no State support, severe cost-cutting and extensive enterprise downsizing (in the short-term at least) (Filatotchev *et al.*, 2000). Researchers usually suggest that all restructuring policies and strategies have to be applied cautiously to transition economies, taking into account country-specific factors. Thus, performance indicators, identified as negative for this study (e.g. the percentage of sales bartered or the percentage of wages paid non-monetarily), may in fact indicate positive economic processes in post-privatised firms, thus implying that these enterprises are functioning and production at least continues.

As for the *Governance – Strategy* hypothesis testing, enterprise size and industrial sector variables were included into *Strategy – Performance* regressions, together with the "part of the larger enterprise" and the "foreign investments in enterprise" controls, to hold non-hypothesised influences constant. Highly significant and positive signs on the size control indicate that in larger firms in the considered sample, performance is better. In particular, exports and the volume of production are generally higher. At the same time, capacity utilisation is lower in larger enterprises, and non-cash wage payments also prevail.

The coefficients for the part of the larger enterprise and the foreign investments in enterprise controls are mostly insignificant, except the two weakly and negatively significant (at the 10% level): one for the percentage of sales exported within the CIS (in relation to the foreign investments in enterprise); and the other for the percentage of sales bartered (in relation to the part of the larger enterprise). These associations could imply

that the barter form of sales is more typical of firms, comprising parts of larger enterprises, and foreign investments are fairly likely to go into enterprises exporting within the CIS.

The introduction of legal company forms (open JSCs, closed JSCs, and partnerships) as controls in the *Strategy – Performance* regression equations did not produce any significant relationships on either the positive or negative side, and also did not show any improvement in terms of the total fit of the model. Thus, they are not reported here.

In order to summarise these decidedly mixed results for *Hypothesis 2*, Table 15 shows the outcomes on all significant coefficients relating *strategies* with *performance*.

Table 15. Summary, Hypothesis 2 Test Results

	Supported for One Indicator	Rejected for One Indicator
With Positive Performance Indicators		
Wage Share of Production Costs	√	
Training Share of Production Costs	√	
Proportion of Total Range of Benefits Received (Administrative Workers)		√
Initial Training	√	
Increase in Training	√	√
Unpaid Leave	√	
Layoffs	√	√√
With Negative Performance Indicators		
Proportion of Total Range of Benefits Received (Administrative Workers)		√
Proportion of Total Range of Benefits Received (Regular Workers)	√	
Initial Training	√	
Training to Upgrade		√
Increase in Training		√√√
Layoffs		√

Hypothesis 2 proposes a positive association between firms' *strategies* that promote employee welfare, and improved corporate *performance*. Like much previous research

(e.g. see Fey and Björkman, 2001), the results summarised in Table 15 are very mixed and certainly do not permit the confirmation/rejection of *Hypothesis 2* straight away, although some of the associations provide preliminary support for our hypothesis. Firstly, as with the *Governance – Strategies* tests, this ambiguity may be attributable to the choice of regression variables that were taken from the particular one-year performance indicators of the ILO questionnaire. Alternatively, one cross-section of data may be insufficient to produce consistent patterns of results.

However, despite speculation on causation in relation to employee-friendly strategies, some of the results show possible improvement in the overall situation in Russia. For example, the result with higher wage payments reflects improved export performance, for CIS exporters at least. As already mentioned, wage payments in enterprises exporting outside the CIS are generally higher than in firms exporting within the CIS. This outcome may result from the competitive environment, which usually is tighter outside CIS countries, thus implying that goods exported there are of a better quality (and are in demand) than those coming to domestic (the CIS) markets. This could be the reason why workers in enterprises exporting outside the CIS are better paid. One of the implications of this result could be a need for retooling of production with the aim to overcome the constraint represented by inert CIS markets, leading to the production of goods, competitive on international markets. (Admittedly, this technological strategy requires substantial investments, and is beyond the focus on HRM strategies in this study.) Among other strategies promoting employee welfare and associated with improved enterprise performance are the increased share of wages as proportion of production costs and less unpaid leaves.

Despite the hypothesised positive association between training strategies and firm performance, various training variables (increase in training, training to upgrade) are both supportive and unsupportive for *Hypothesis 2*. It is generally recognised that specific strategies, relating to employee welfare within firms (like wage levels or spending on training), have a long tradition within the FSU, where the quality and skills of hired individuals were enhanced through comprehensive training provided. However, our analysis shows that when the increase in training (positive performance association) is supported by the results, it is at the same time rejected by (three) negative performance

indicators. The same contradictory situation occurs with layoffs that are variously positively and negatively associated with performance in our findings. At the same time, it has to be remembered that during times of economic stress, layoffs could occur not only because of low skill levels, but also for strategic reasons (Hoskisson *et al.*, 1994).

The ambiguity of results that is specified by positive and negative performance indicators may first be attributed to the choice of negative performance indicators, as was already noted. However, bearing in mind that workers with low productivity or low skill levels usually could be easily replaced from the pool of unemployed, and the positive and significant association between layoffs and the percentage of sales exported may simply indicate that growing exports require a more qualified work force, which however comes from outside rather than being trained within the enterprises. Also, the higher is the volume of production, the more layoffs occur – new, qualified workers may replace those with poor skills.

Although this explanation sounds reasonable, some Western research on Russia and most of the FSU indicates that the in-house form of training is more traditional for Russian enterprises, at least when it is not too costly. The positive association between initial training and improved firm performance supports this notion with two kinds of performance indicators. As described, this may indicate a rise in the demand for qualified employees in fast growing or expanding Russian enterprises.

The results presented so far in relation to individual HRM strategies have been, frankly, disappointing. However, one (suggested) productive line of enquiry may lie on the combination of individual strategies into meaningful strategic bundles. The next Section provides the results of statistical tests on *Governance – Strategy – Performance* relationships in terms of the three coherent strategic bundles, developed from the Western literature for this Russian research.

5.5 COMPOSITE HRM STRATEGIES

In the Fey and Björkman (2001) study of *Strategy – Performance* links in Russian enterprises, different HRM practices for managerial and non-managerial workers were reported to be positively and significantly associated with enterprise performance. The authors constructed three HRM composite variables for employees, which include *Employee Development*, *Feedback Systems* and *Pay/Organisation*. Besides Fey and Björkman (2001), Western research provides examples of other strategic HRM bundles of clusters, developed in particular by Baron *et al.* (1996, 1999); Hannan *et al.* (1996); Berger and Huselid (1996); MacDuffie (1995); Osterman (1999, 2000; Spenner *et al.* (1998). It was also noted by Ngo *et al.* (1998) that there is only limited theoretical guidance on precisely how HRM practices should be bundled together, so in this research we follow the above authors and conceptualise the constructs according to the established theoretical expectations (see Section 3.3 above). Thus, the three coherent HRM strategies identified comprise *Traditional Social Welfare (TSW)*, *Cost Minimisation (CM)* and *Human Resource Investment (HRI)*.

It is proposed that these HRM strategies divide the sample into three distinctive groups of firms, according to the extent to which the strategic choices of a firm are dominated by a particular strategy. For a predetermined number of clusters (n = 3 in this case), k-means cluster analysis[6], following the k-means clustering algorithm of Hartigan (1975), is used here to identify homogenous subgroups, which both minimise within-group variation and maximise between-group variation. To confirm that the above strategies discriminate well

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[6] K-means cluster analysis uses Euclidian distance and attempts to identify relatively homogeneous groups of cases based on selected characteristics. Initial cluster centres are chosen in a first pass of the data, then each additional iteration groups observations based on nearest Euclidian distance to the mean of the cluster. Thus cluster centres change at each pass and the process continues until cluster means do not shift more than a given cut-off value or the iteration limit is reached.
Euclidian distance is the distance measure, where a given pair of cases is plotted on two variables, which form the *X* and *Y* axes. The Euclidian distance is the square root of the sum of the square of the *X* difference plus the square of the *Y* distance (Garson, 2001).

between the obtained bundles, stepwise discriminant analysis[7] was performed together with ANOVA[8] on each composite strategy variable.

Table 16 below presents the results of cluster analysis that shows that these three strategic centroids are statistically distinctive. In particular, for firms dominated by *Traditional Social Welfare* strategies, the *TSW* bundle shows quite a high value for the *TSW* composite variable (0.802), a negative value for *CM* (-0.482) and a low value for the *HRI* strategy (0.301). Firms dominated by *HRI* strategies (*HRI* bundle) show low values for *CM* (0.273) and negative values for *TSW*, but for the *HRI* strategy this value is negative and high (-0.848). For the *CM* bundle the corresponding *Strategic Options* values are either low or negative. In the ANOVA results below, the smaller the Wilks' lambda, the more important the dependent variable to the discriminant analysis. Wilks' lambda is significant by the F-test for all variables and thus confirms the significance of the differences.

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[7] Discriminant analysis is used to classify cases into the values of a categorical dependent (usually dichotomous) with a purpose to investigate differences between groups, to reject variables which are little related to specific groups, to classify cases into groups and to test whether cases are classified as predicted (Garson, 2001).

[8] ANOVA (analysis of variance) is used to uncover the main and interactive effects of categorical independent variables (factors) on an interval dependent variable. The key statistic in ANOVA is the F-test of difference of group means, testing if the means of the groups formed by values of the independent variable are different enough not to have occurred by chance. If the group means are not significantly different, then it is inferred that the independent variable(s) did not have an effect on the dependent variable (Garson, 2001).

Table 16. HRM Composite Strategy Variables and Firm Clusters

	Cluster Means (standard deviation)			ANOVA		
	TSW Bundle	*CM* Bundle	*HRI* Bundle	Wilks' Lambda	F	Sig.
TSW Strategic Option	0.802 (0.43)	-0.268 (0.36)	-0.524 (0.37)	0.211	328.449	0.000
CM Strategic Option	-0.482 (0.36)	0.205 (0.49)	0.273 (0.69)	0.123	270.016	0.000
HRI Strategic Option	0.301 (0.56)	0.585 (0.41)	-0.848 (0.38)	0.116	187.361	0.000
N	98	96	101			

From the results of cluster analysis it is possible to draw another important conclusion. All three *TSW*, *CM* and *HRI* strategic bundles have not been found to be ultimately and exclusively dependent on respectively *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* strategies. Although one strategy dominates, some elements of the other two alternatives are always present. This may be important from the theoretical perspective and is consistent with firms' "strategic experimenting" in the form of mixed HRM strategies, described in Subsection 3.3.4. However, we noted *ibid* that the process of mixing (or sequencing) HRM strategies is a balancing act between initiating actions that follow one strategy and then deviating from that strategy. It usually also takes years and highly skilled management to fully implement one strategy, before changing to another one, so with the real possibility that Russian managers may not be qualified well to promote these advanced, mixed strategies, and due to the constraints imposed by only one cross-section of data available, the issue of "strategic experimenting" is beyond the bounds of this thesis.

5.5.1 GOVERNANCE – STRATEGY

A number of hypotheses were generated concerning composite strategies in relation to governance (see Section 3.3), analysed with heteroskedasticity-adjusted OLS regressions [9] and [10], described in the relevant chapter above. In particular, these hypotheses include *Hypothesis 3*, *Hypothesis 5* and *Hypothesis 7*.

Following the theoretical discussion, many firms, rather than trying to adopt new strategies under transition, usually simply follow their founders' initial template for employment relations (Baron, *et al.*, 1999). In Russia, many of the post-privatised firms also used the founders' traditional Soviet-style strategy, which primarily was based on lifetime employment, provision of many of the social needs of both current and retired employees, thus amounting to paternalism by corporations. For these reasons, and bearing in mind that workers and managers represent the main group of owners of Russian enterprises, *Hypothesis 3* proposes that higher levels of insider ownership will be positively associated with higher levels of *TSW* provision for employees.

At the same time, increased outside ownership and control, and withdrawal of the State, with its traditional system of social provision, faced many firms with the need to minimise social costs within recent years. The above discussion suggests that under this strategy (i.e. *CM*) employees, as shareholders, could win, but as employees (concerned with their personal welfare and job stability, rather than the value of enterprise shares), they are more likely to lose. Remembering that the role of shareholders is rather new for Russian employees, they are more likely to oppose any strategy that reduces their stability as employees. Thus, contrary to *Hypothesis 3*, *Hypothesis 5* suggests that lower levels of insider ownership could be associated with active *Cost Minimisation* strategies in Russian firms.

The last specific HRM hypothesis (*Hypothesis 7*), developed for *Governance – Strategy* examination, is founded on high-commitment "psychological contracts" between firms and workers, who contribute efforts on behalf of the firm that exceed any contractual obligations (Guest, 1998). This strategy may result in efficiency gains for enterprises

(Barberis *et al.*, 1996; Buck *et al.*, 2003; Fey and Björkman, 2001). Thus, *HRI* strategies may promote value for insider shareholders and short term utility for employees. Therefore, we hypothesise that higher levels of insider ownership will be positively associated with the intensity of high-commitment *Human Resource Investments*.

Table 17 presents the tests on these three hypotheses. It can be seen that the results for workers' ownership in relation to *TSW* strategy are inconsistent with *Hypothesis 3*, as this association is only weakly significant at the 10% level.

Table 17. Governance – Strategies

	Traditional Social Welfare	Cost Minimisation	Human Resource Investment	Traditional Social Welfare	Cost Minimisation	Human Resource Investment
Managers' Shares	-0.061	**-0.068**	-0.046			
	(-1.29)	**(-2.19)***	(-0.80)			
Workers' Shares	**0.087**	**-0.097**	0.064			
	(1.75)†	**(-2.96)****	(1.04)			
Legal Forms:						
Partnership				-0.029	-0.005	-0.015
				(-1.07)	(-0.20)	(-0.36)
Closed JSC				-0.015	-0.028	0.038
				(-0.50)	(-1.26)	(0.98)
Open JSC				0.017	-0.004	0.050
				(0.65)	(-0.19)	(1.54)
Controls:						
Ln Employment	**0.039**	0.004	**0.028**	**0.056**	-0.001	**0.053**
	(3.17)**	(0.43)	**(1.81)†**	**(8.71)****	(-0.12)	**(6.24)****
Part of Larger Enterprise	0.00005	0.011	-0.027	-0.026	-0.008	-0.002
	(0.00)	(0.26)	(-0.35)	(-0.92)	(-0.37)	(-0.05)
Food	**-0.080**	**-0.055**	**0.136**	**-0.047**	**-0.035**	**0.106**
	(-2.04)*	**(-2.14)***	**(2.81)****	**(-1.70)†**	**(-1.72)†**	**(3.17)****
Light	0.026	0.016	**0.110**	0.022	**0.033**	**0.067**
	(0.77)	(0.69)	**(2.63)****	(1.04)	**(1.82)†**	**(2.49)****
Wood & Paper	0.019	-0.067	0.092	0.022	**-0.048**	**0.080**
	(0.27)	(-1.45)	(1.05)	(0.62)	**(-1.82)†**	**(1.54)†**
Chemistry	-0.073	-0.004	0.068	0.006	-0.022	**0.113**
	(-1.58)	(-0.12)	(1.20)	(0.18)	(-0.92)	**(2.51)****
Construction Materials	-0.040	-0.024	0.081	-0.052	-0.028	0.543
	(-0.74)	(-0.66)	(1.20)	(-1.48)	(-1.26)	(1.10)
Constant	**0.196**	**0.419**	**0.213**	**0.080**	**0.406**	0.024
	(2.35)*	**(7.63)****	**(2.07)***	**(1.99)***	**(12.82)****	(0.47)
Observations	128	128	128	295	295	295
R-squared	0.26	0.15	0.13	0.27	0.06	0.17
F-statistics (Prob>F)	4.64	2.38	1.97	13.19	2.18	7.72
	(0.000)	(0.017)	(0.042)	(0.000)	(0.019)	(0.000)

Robust t-statistics in parentheses

† significant at 10% level; * significant at 5% level; ** significant at the 1% level

As was hypothesised in *Hypothesis 5*, low levels of insider ownership (MO and WO) are significantly and negatively associated with active *Cost Minimisation* strategies. The result

is significant with both kinds of employees (managers and workers) refusing to support strategies that reduce their wages or other traditional benefits available.

Finally, the results for high commitment *Human Resource Investment (HRI)* strategies, hypothesised to be positively associated with higher levels of insider ownership, provide no significant evidence in support of *Hypothesis 7*.

As opposed to share ownership parameters, legal forms of enterprises for all three specific *Governance – Strategy* hypotheses (not reported in detail) prove to be insignificant. It will be argued later in this Section that legal forms have only a nominal influence on firms' HRM strategies, in the considered sample at least.

As for tests on *Hypothesis 1* and *Hypothesis 2*, a number of control variables were included in the regressions, to hold the non-hypothesised influences constant. Highly significant (at the 1% level) and positive signs on the size control variable indicate that *TSW* and *HRI*, as welfare strategies, are more typical of larger firms in the considered sample. At the same time, the Food industry exhibits the highest number of significant coefficients. In particular, *HRI* investments may be generally accepted, whereas *TSW* and *CM* may be significantly opposed, by most of the Food industry employees.

It has to be noted that, as for the *Governance – Strategy* tests in terms of *Hypothesis 1*, the considered sample for *Hypothesis 3*, *Hypothesis 5* and *Hypothesis 7* estimations was restricted to those firms (128 out of the 295 sampled for this study), where ownership may be expected to change, i.e. open and closed JSCs. These restrictions follow Djankov and Murrell (2002), and are presented in Section 5.3 above and not reported here.

Table 18 below summarises the above discussion for HRM specific *Governance – Strategy* hypotheses for both different ownership structures and various legal forms examined.

Table 18. HRM Governance – Strategy Hypotheses Test Results

	Supported for One Indicator	Rejected for One Indicator
For Different Ownership Structures		
Hypothesis 3		√
Hypothesis 5	√√	
Hypothesis 7		√
For Different Legal Forms		
Hypothesis 3		√
Hypothesis 5		√
Hypothesis 7		√

Our results shows that both *Hypothesis 3*, which predicts a positive association between higher levels of insider ownership and higher levels of *TSW* provision for employees (as a result of such association), and *Hypothesis 7*; predicting that higher levels of insider ownership are positively associated with the intensity of high-commitment *HRI*, are insignificant and provide no evidence for these associations in Russian enterprises.

Only *Hypothesis 5*, which associates lower levels of insider ownership with active *CM* strategies, is supported, since the obtained coefficients are significant and show that managers and other employees refuse to support strategies that reduce their wages or other traditional benefits available. So, although downsizing and cost cutting, as HRM policies, are popular strategies in the West (being highly recommended by Western economic advisors for Russia too), they do not seem appropriate for Russian employees, more concerned with their personal welfare and job stability, rather than enterprise value. Employees therefore oppose *CM* strategies as personally damaging their welfare (Fernandez and Rodrik, 1991, Filatotchev *et al.*, 2000). Interestingly, this result shows that the *CM* strategy may be opposed by both groups of insiders – managers and workers. If managers are hired from outside, they may be more focused on raising shareholder value for the firm. However in our firms, managers are also likely to act as employees, rather than shareholders, and care about their personal welfare, though the effects of *CM* (and other strategies) on performance are yet to be examined.

The result for the *TSW* strategic bundle suggests, that having already become a rather unfashionable business strategy in Western firms (Wray, 1996), the former Soviet-style, paternalistic template of employee relations seems also to be ill-suited for the post-privatisation Russian environment. (However, the 10% significance level of association between *TSW* and WO might indicate that this strategy is still popular in some of the considered enterprises.) Thus, the main outcome of these three individual HRM strategies suggests that insider ownership is negatively associated with the composite *CM* strategy, that directly opposes employee welfare, in the short run at least.

For various legal company forms, all three *Governance – Strategy* hypotheses, described above, provide very low levels of significance in terms of the specific HRM approaches, and thus were rejected. This finding can be interpreted in the way that the described legal structures have only nominal influence on firms' CG and HRM strategies, and act rather as cosmetic devices in Russian enterprises, superimposed on existing competences and routines. (Similar findings were obtained by Spenner *et al.* (1998) for Bulgaria). Similar results have already been described in this Chapter for individual benefits (see Tables 11 and 12 in Section 5.3), where the legal forms of enterprises were found to have no significant association with benefit strategies (except for the single association between the remuneration system and the partnership form of governance, Table 12).

Regardless of these speculations, and following these *Governance – Strategy* findings, it is in any case interesting to establish which of the three hypothesised *Strategy – Performance* models is associated with improved firm performance. The next Section tries to provide the answers.

5.5.2 Strategy – Performance

Following the *Governance – Strategy* examination, based on *Hypothesis 3*, *Hypothesis 5* and *Hypothesis 7*, this Section proposes to test *Strategy – Performance* relations with the three HRM bundles. This estimation is based on *Hypothesis 4*, *Hypothesis 6* and *Hypothesis 8*, developed and justified in the theoretical Section 3.3 above.

In particular, consistent with *Hypothesis 2* in relation to aggregate HRM strategies and firm performance, and based on the grounds discussed for traditional "Soviet" HRM system of welfare provision, we continue to assume that the provision of *TSW* benefits in the FSU is uniquely suited to the national culture and institutions in Russia. Thus we hypothesise (*Hypothesis 4*) that firm performance is positively associated with *TSW* provision for employees.

It is also assumed that any form of cost-cutting in relation to employment stability and employee welfare runs contrary to the national culture, philosophy and institutions of Russia. So, contrary to the *TSW* strategy, and following the Ukrainian study by Buck *et al.* (2003) and by Spenner *et al.* (1998) on Bulgarian companies, the strategy identified here as *Cost Minimisation* is expected to have a negative effect on organisational performance. Hence, under the influence of private inside owners, we hypothesise that firm performance is negatively associated with "hard" *CM* strategies – *Hypothesis 6*.

Subsequently, following Fey and Björkman (2001), who empirically showed that *Human Resource Investment* strategies in foreign subsidiaries in Russia are positively associated with improved firm performance, and Buck *et al.* (2003), who found a similar association for high-commitment HR strategies in Ukraine, we hypothesise (*Hypothesis 8*) that firm performance is positively associated with new *HRI* investments.

Table 19 below presents the results of the proposed *Strategy – Performance* analysis in relation to *Hypothesis 4*, *Hypothesis 6* and *Hypothesis 8*. For these tests the full sample is used and the analysis is based on regression [11] and logistic equation [12]. As for the first (general) approach, two sets of performance indicators consist of positive and negative ones, as described in Section 4.3, where percentage of sales exported within the CIS, percentage of sales exported outside the CIS, capacity utilisation and increase in volume of production were introduced as positive performance indicators; and percentage of wages paid non-monetarily, percentage of sales bartered and bankruptcy threat as negative performance indicators.

Table 19. Strategies and Firm Performance (Robust Regression; LOGIT where indicated)

	Positive Performance Indicators				Negative Performance Indicators			
	% of Sales Exported Within the CIS, 1999	% of Sales Exported Outside the CIS, 1999	Capacity Utilisation	Increase in Volume of Production (LOGIT)	% of Wages Paid Non-monetarily/ Workers	% of Wages Paid Non-monetarily/ Engineers	% of Sales Bartered, 1999	Bankruptcy Threat (LOGIT)
Traditional Social Welfare	0.023	0.071	12.071	0.934	**0.248**	0.140	0.004	-0.256
	(0.64)	(1.48)	(1.01)	(0.92)	**(2.70)****	(1.49)	(0.07)	(-0.15)
Cost Minimisation	0.033	-0.011	-3.098	-0.501	-0.018	0.022	-0.059	2.411
	(0.73)	(-0.19)	(-0.21)	(-0.41)	(-0.15)	(0.19)	(-0.77)	(1.04)
Human Resource Investment	-0.031	**-0.071**	**29.651**	**5.000**	**0.110**	0.081	0.052	**-3.822**
	(-1.18)	**(-2.02)***	**(3.35)****	**(6.51)****	**(1.62)†**	(1.17)	(1.17)	**(-2.83)****
Controls:								
Ln Employment	**0.016**	**0.013**	**-4.490**	0.101	**0.031**	**0.033**	**0.013**	0.143
	(3.78)**	**(2.24)***	**(-3.08)****	(0.79)	**(2.75)****	**(2.87)****	**(1.70)†**	(0.62)
Part of Larger Enterprise	-0.026	-0.021	8.714	-0.447	-0.025	0.002	**-0.054**	-0.199
	(-1.49)	(-0.90)	(1.48)	(-0.91)	(-0.56)	(0.04)	**(-1.83)†**	(-0.18)
Food	-0.022	-0.003	-3.011	0.563	**0.067**	**0.069**	-0.027	-0.546
	(-1.47)	(-0.15)	(-0.60)	(1.23)	**(1.75)†**	**(1.75)†**	(-1.06)	(-0.46)
Light	**-0.023**	0.011	**7.976**	0.162	0.025	0.007	0.010	0.224
	(-1.85)†	(0.68)	**(1.90)†**	(0.45)	(0.77)	(0.21)	(0.49)	(0.33)
Wood & Paper	-0.007	**0.013**	0.913	-0.398	0.016	0.007	-0.012	0.471
	(-0.33)	**(4.63)****	(0.13)	(-0.71)	(0.30)	(0.12)	(-0.35)	(0.40)
Chemistry	-0.005	**0.046**	-6.195	-0.271	0.028	0.020	0.042	**1.563**
	(-0.28)	**(1.91)†**	(-1.01)	(-0.55)	(0.58)	(0.41)	(1.35)	**(1.97)***
Construction Materials	-0.022	-0.008	1.364	-0.736	-0.004	0.013	0.052	0.004
	(-1.15)	(-0.30)	(0.21)	(-1.18)	(-0.08)	(0.26)	(1.56)	(0.00)
Constant	**-0.063**	-0.050	**67.742**	**-2.376**	0.023	0.020	-0.007	**-3.417**
	(-2.12)*	(-1.28)	**(6.81)****	**(-2.66)****	(0.31)	(0.26)	(-0.15)	**(-1.81)†**
Observations	292	292	290	295	293	293	292	295
R^2 [LOGIT: PseudoR^2]	0.10	0.12	0.09	0.20	0.14	0.09	0.06	0.10
F-statistics (Prob>F) [LOGIT: Wald Chi-square (Prob>Chi-square)]	3.28	4.00	2.82	64.25	4.62	2.88	1.81	15.87
	(0.001)	(0.000)	(0.002)	(0.000)	(0.000)	(0.002)	(0.059)	(0.091)

Robust t-statistics (Robust Z-statistics for LOGIT) in parentheses; † significant at 10% level; * significant at 5% level; ** significant at the 1% level

Contrary to the *Governance – Strategy* analysis in Subsection 5.5.1, and taking into account this specific composite strategy approach, our three strategic bundles were included as independent – as opposed to dependent in the earlier analysis – variables in regressions to test the hypothesised associations.

Table 19 shows that of five significant (at the 5% level or better) coefficients, only three are of the hypothesised sign, and two oppose the above hypotheses. At that, the results for the *HRI* strategy are quite consistent with Fey and Björkman (2001) findings for the performance of foreign subsidiaries in Russia, but otherwise, they are fairly insignificant.

In particular, looking at "soft", *TSW* strategies, there is only one significant outcome, which is the positive association (significant at the 1% level) between this *TSW* bundle and the proportion of wages paid non-monetarily (a negative performance indicator). Thus *Hypothesis 4* is not supported, and is rejected in relation to non-money wages. Perhaps, as discussed above, this latter variable may be viewed not as a negative performance outcome, relevant to employee shareholdings, but as just another feature of the *TSW* strategy itself, whereby enterprise managers tie employees to the firm with high-commitment HRM, but then exploit employees to some extent by under-investing in marketing resources, not paying money wages, and essentially giving employees the marketing problem of disposing of enterprise outputs.

Second, results for the *CM* strategic bundle are uniformly insignificant, and provide no support whatsoever for *Hypothesis 6*. This is consistent with all kinds of speculative explanations, but the truth is that this result still represents a major mystery and an interesting area for further research. Besides, it also has to be remembered that the *CM* strategy may have been opposed by all groups of Russian insiders.

Third, however, the high-commitment *HRI* strategy shows fairly consistent and significant results, with only one exception. In terms of two positive performance indicators (capacity utilisation at the 1% level of significance, and increase in production volume at the 1% level of significance) and one negative performance indicator (bankruptcy threat at the 1% level), the *HRI* strategy shows a positive association with the enterprise performance, and to this extent *Hypothesis 8* is supported. However, *HRI* is also significantly (at the 5%

level) and negatively associated with export sales outside the CIS (though not within the CIS), and this contravenes this hypothesis. Interestingly, *HRI* strategies are positively associated with production-side performance measures (capacity utilisation, increase in production), but not export sales outside the CIS. This is reminiscent of experiences with earlier, centrally-planned enterprises, whose strategies could raise output but generally not quality of goods and services capable of competing on world markets.

Although the *HRI* strategy obviously involves extra costs for the firm, in terms of additional training costs, etc., it may be an important result that the bankruptcy threat (a negative performance indicator) is significantly and negatively associated with *HRI*, an outcome consistent with *Hypothesis 8*. With the exception of exporting outside the CIS, these results for *HRI* are broadly consistent with the earlier results of Fey and Björkman (2001).

Referring to the controls introduced for *Strategy – Performance* tests, firm size is mostly significantly related with firm performance, indicating that larger firms slightly outperform smaller firms in exporting, volumes of barter exchange and payment of wages (though in non-monetarily form). Following Fey and Björkman (2001), it is also encouraging that the order (in terms of size) in which the HRM bundles are correlated with firm performance is consistent with the order (in terms of size) of the betas in the regression equations.

The following Table summarises the above discussion and distributes the three HRM *Strategy – Performance* hypotheses in relation to results.

Table 20. HRM Strategy – Performance Hypotheses Test Results

	Supported for One Indicator	Rejected for One Indicator
Hypothesis 4		√
Hypothesis 6		√
Hypothesis 8	√√√	√

So, *Hypothesis 4*, stating that firm performance is positively associated with *TSW* provision for employees, is not supported at all and is rejected in relation to non-money wages. *Hypothesis 6*, which hypothesised a negative relationship between firm performance and *CM* strategies, is also rejected since the obtained results provide no evidence for this hypothesis, and the associations between the *CM* strategic bundle and different performance measures are uniformly insignificant. This insignificant outcome may not be without importance, however, and this is discussed in the final Chapter.

Only *Hypothesis 8*, predicting a positive association between firm performance and new HRM investments, shows fairly consistent and significant results for both of the hypothesised associations – a negative performance indicator is significantly and negatively associated with *HRI*, and positive performance indicators are significantly and positively associated with *HRI*.

5.6 CONCLUSION

This Chapter has provided the main findings from the tests of the eight hypotheses, proposed for this *Governance – Strategy – Performance* research. These results will be addressed further in the next Chapter, which presents a Discussion and Future Work suggestions.

Following the theoretical discussion of the Russian post-privatisation environment and Western strategies applicable for the FSU in general, the hypothesised associations between firm *governance* and *strategies* were established using such CG parameters as insiders' ownership proportions and legal forms of the enterprises. Subsequently, with the main interest of this research on employee welfare in Russian industrial firms, the association between *strategies* and *performance* focused on HRM strategies only. In particular, one of the approaches adopted here included hypothesis testing with the use of three distinctive HRM bundles, comprising *Traditional Social Welfare (TSW)*, *Cost Minimisation (CM)* and *Human Resource Investment (HRI)* strategies. Until recently, these bundles (or their modifications) have been identified mostly with research on high

technology Silicon Valley firms (e.g. see Baron *et al.*, 1996). Besides, Buck *et al.* (2003) used similar strategic bundles for their Ukrainian study, and also Fey and Björkman (2001), who examined *Strategy – Performance* relationships in foreign subsidiaries in Russia (with *Employee Development*, *Feedback Systems* and *Pay/Organisation* bundles).

Like much previous research, our results are quite mixed and do not permit the immediate confirmation or rejection of our hypotheses. To guide the reader through our findings, four summary tables were introduced to review the outcomes. Leaving numerous discussions on revealed associations for the relevant sections below, we present only some core findings here.

In particular, in Section 5.3 (see summary Table 13) it was found that in terms of *Governance – Strategy* mechanisms, transfers of funds into various benefits and bonus payments were significantly associated with worker ownership. Specifically, this could imply that workers impose discipline on managers to choose strategies that immediately favour employees. Within the *Strategy – Performance* analysis (see summary Table 15 in Section 5.4), the results are more mixed (and frankly disappointing), although some of them nevertheless suggest that some possible improvements in the overall situation in Russia have occurred. For example, higher wage payments were associated with improved export performance, for CIS exporters at least.

In terms of the proposed HRM approach, probably the only firm conclusion that can be drawn from the outcomes, based on individual HRM strategies (see summary Table 18, Subsection 5.5.1), is that insider ownership seems to have no consistent association with individual strategies that benefit or do not damage employees (i.e. on either *TSW* or *HRI*). However, insider ownership is negatively associated with the composite *CM* bundle, that directly reduces employee welfare, in the short run at least. It also seems that, on average, Russian enterprises are not homogeneous in terms of implemented HRM strategies. Perhaps they are trying to experiment with them, applying experience from Western enterprises in the context of current performance.

Besides, our results also suggest (see summary Table 20, Subsection 5.5.2) that high commitment HRM, in its new *HRI* form ("harder" than the old paternalism of traditional

TSW), is a strategy that is broadly associated with positive performance outcomes in Russian industrial firms, as previously found by Fey and Björkman (2001).

Although many other results are mixed, they still provide a rich basis for discussion at greater length in the final Chapter.

CHAPTER VI. Discussion and Future Work

6.1 General Overview

This thesis presented an empirical examination of the relationships between corporate governance, strategies in relation to employee welfare and firm performance in Russian post-privatisation firms. A number of tests have been designed for the hypothesised associations.

This study started with the examination of the situation in Russia after the mass privatisation programme, carried out between late 1992 and 1994 for most manufacturing firms. Russian MPP, as part of other economic and political reforms, was expected to replace the State in corporate governance with more effective owners and enterprise monitors. Hopes were entertained that improved CG would lead to appropriate strategic choices, especially in relation to human resources, arguably the most valuable asset of Russian firms. This in turn could lead to an increased capability of firms to compete on world product markets. However, for the bulk of privatised manufacturing firms the outcome has been in the form of "employee-owned, manager-controlled" enterprises (Earle and Estrin, 1996), with only limited roles for outside investors. This created a danger that insider ownership by managers and workers may favour decisions that promote their own immediate sources of utility, and subsequently undermine the firm's financial performance and value in the long term.

Through the definition of the research model, adopted from the field of Strategic Management, and formulation of the main sets of the research questions, it was argued that this thesis is an extension of two antecedent empirical studies on the FSU, one by Buck *et al.* (2003) on the influence of governance forms on HRM strategies in Ukraine, and another by Fey and Björkman (2001) on *Strategy – Performance* relations in foreign subsidiaries operating in Russia. The originality of this research lies in the supplementation of the *Strategy – Performance* approach of Fey and Björkman (2001) with a consideration of associations between *Governance – Strategy – Performance* on a

sample of indigenous Russian firms. In comparison with Buck *et al.* (2003), it studies Russia, as the most developed State after the collapse of the Soviet Union (EBRD, 2001). This offers the opportunity to generalise findings to the FSU as a whole. In addition it uses legal form governance variables, and alternative performance measures to the quantitative measures used by Buck *et al.* (2003): capacity utilisation and sales per employee. Fey and Björkman (2001) argue the case for subjective performance measures. This thesis endorses their view and extends it by using negative performance measures, such as perceived bankruptcy threats and barter trading.

An extensive analysis of the existing literature provided a detailed review of theories and previous empirical findings on *Governance – Strategy – Performance* relations, with the most interest paid to the FSU and other transition economies. In terms of the proposed *Governance – Strategy – Performance* model, this thesis focused on ownership proportions and legal company forms as two *governance* elements associated with HRM *strategy*, and on HRM *strategies* as a key bundle of strategy parameters, associated with firm *performance*. This analysis identified important gaps in the literature in relation to transition research, and set the stage for this study to contribute to filling these gaps and contributing to knowledge by examining Russia-specific CG and HRM strategies. In particular, three strategic HRM bundles, derived from Western theory, were identified as appropriate for Russia: *Traditional Social Welfare (TSW)*, *Cost Minimisation (CM)*, and *Human Resource Investment (HRI)*.

With regards to methodology, this thesis followed some of the previous studies on transition and Western economies, and implemented methods of correlation and regression analysis (OLS and LOGIT) for tests on individual HRM elements, and methods of cluster analysis for examination of *Governance – Strategy – Performance* in terms of the three HRM strategic bundles.

No attempt is made here to argue that this thesis fills all research gaps or finds the final answer to important research questions. The results of some of the tests are admittedly rather mixed, partially confirming and partially rejecting certain associations predicted by

the research hypotheses. The following Section proceeds with the analysis of these findings, and discusses their possible contribution to knowledge.

6.2 INTERPRETATION OF THE RESULTS

The results of tests of the eight main hypotheses were presented in Chapter V. They provide a rich basis for discussions on employee welfare in Russia in the context of *Governance – Strategy* and *Strategy – Performance* mechanisms, various ownership proportions and different HRM practices adopted. At a general level, these results are quite new, though Fey and Björkman (2001) have studied the consequences of high-commitment HRM strategies on firm performance in Russia, though they embraced only foreign subsidiaries operating in Russia. To date there has been no large-sample empirical research on the influence of *governance* forms on different HRM *strategies*, and of a variety of HRM *strategies* on *performance*, so this work has been able to identify some important associations of insider ownership in Russian firms with strategies influencing employee welfare, and has discovered some interesting associations between employee-favouring behaviour of the companies and insider ownership.

As was mentioned in previous Section, this work is based on two approaches – one using individual HRM elements and another using composite HRM bundles. Each of these approaches is used to examine *Governance – Strategy – Performance* associations. When drawing conclusions, it must be remembered that, in reality, many influences on *strategies* and *performance* must have been omitted, *governance* may be expected to have a lagged influence on *strategies*, and *strategies* and *governance* may interact (Buck *et al.*, 2001). This casts doubt on the relevance of methodology, based on a single cross-section of data, and any results must be considered provisional at this stage. Nevertheless, we argue that these provisional results are important and useful for later research.

6.2.1 GOVERNANCE – STRATEGY

While analysing the association between employee-favouring strategies and insider ownership, workers' shareholdings were found to be positively associated (as hypothesised) with the provision of the whole range of benefits. Also, workers' ownership (WO) is significantly associated with remuneration strategies, comprising wages and individual bonuses (though to workers only), which could be interpreted as workers having a consistent influence on remuneration strategies in their enterprises, with managers not seeming to seriously resist these strategies of workers. This result, together with the reported significant associations between workers' ownership and the range of benefits provided, can indicate some improvement in the *governance* in Russian enterprises, where workers, as shareholders, consistently influence certain HRM strategies.

Although it is recognised that successful American and British companies emphasise training and training-associated activities as strategies, resulting in improved company performance (Pfeffer and Veiga, 1999), no form of training was found to be significant among the strategies that direct resources towards employee welfare. Precisely, managers' shareholdings were found to be negatively associated with the provision of training, and also with the provision of the considered range of benefits to employees (like paid vacation, sickness benefit through paid health services, subsidised rent and kindergartens, retirement assistance, etc.). In particular, the results suggest that the provision of training for employees is negatively associated with managerial ownership (MO), and this is consistent with the possibility that training conflicts with managers' immediate interests and is opposed by them. At the same time, WO is not significantly associated with any training strategy at all, thus probably suggesting that the issue is outside workers' competences and influences.

This result for managerial ownership could imply that managers are not likely to invest in intellectual human capital of company employees, although the explanation could come from the choice of employees sampled by the ILO. Particularly, following Brown (1998), workers in the sampled enterprises could have low productivity or skills that are not in

demand, thus the non-provision of training to employees may represent one of managers' cost-saving strategies, in the short run at least.

In relation to benefits provision, it was theoretically justified in earlier chapters that managerial ownership may be associated with benefits for employees exponentially, firstly rising with increasing MO, but then falling, once MO passes some critical (threshold) level. Perhaps also, at low levels of MO, managers feel a need to collude with workers' requests for benefits provision from employees, but, when managers' ownership increases, they feel safe to challenge workers. However, empirical result suggests that coefficients for MO^2 are close to zero, and thus the possible degree of "exploitation" of workers seems negligible.

These results are also consistent with some conflict of interests between workers and managers, both acting as shareholders, but perhaps favouring different strategies. However this difference is disputable if one looks at the results for composite strategic variables rather than individual elements of HRM strategies. Here, insider ownership (MO and WO) is found to be negatively associated with active *Cost Minimisation* strategies. Interestingly, this result is consistent with both kinds of insiders (managers and workers) refusing to support strategies that cut their traditional benefits, reduce their wages or eliminate jobs. Following Fernandez and Rodrik (1991) and Filatotchev *et al.* (2000), Russian employees oppose a *CM* strategy (popular in the West and recommended by Western economic advisors for Russia) as damaging to their individual welfare. It was already noted that once *CM* is opposed by both workers and managers, this implies that managers are likely to act as employees, rather than shareholders, and care about their personal welfare. This negative association between *CM* strategy and insider ownership is also supported by Buck *et al.* (2003) findings on the Ukrainian firms, where high degrees of insider ownership were found to be negatively associated with cost-cutting strategies. Together with similar results for Russia, this is highly suggestive of a universal mechanism in the FSU as a whole.

While Russia's national culture of high uncertainty avoidance (Elenkov, 1998) was assumed to favour traditional form of employment relationship, the result for the *TSW*

strategic bundle suggests, that this paternalistic, former Soviet-style template seems now to be ill-suited for the post-privatisation Russian environment, as it has already become in Western firms (Wray, 1996). However, the 10% significance level of association between *TSW* and WO might indicate that this strategy is still popular in some of the sampled enterprises.

In relation to the institutional feature of different legal forms of the enterprises, no influence was found on the proportions of benefits received, wage, training and social cost shares of production costs, layoffs and various forms of training. The *Governance – Strategy* hypotheses provided very low levels of significance in terms of the specific HRM bundles (and thus were rejected), and similar results were obtained for individual HRM approach, where the legal forms of enterprises were found to have no significant association with benefit strategies. Only the partnership form of governance was significantly associated with the presence of a remuneration system with basic wages and monthly bonuses and of training to upgrade, negatively in each case. These findings can be interpreted as indicating that legal forms in Russia have only a nominal influence on firms' actual HRM strategies and CG, and act as cosmetic devices, superimposed on existing competences and routines (Spenner *et al.*, 1998). This result vindicates the decision of Buck *et al.* (2003), made without recourse to the evidence, to exclude legal forms as *governance* variables. It would appear that significant associations between ownership and HRM strategies arise regardless of legal form. This is a strong result, suggesting, for example, that closed or open JSCs make little difference to chosen strategies.

Probably the only conclusion that can be made from all these diverse outcomes for *Governance – Strategy* associations, is that insider ownership seems to have no consistent association with individual strategies that benefit employees. On the other hand, HRM strategies cannot be chosen as individual items from a long menu (Baron *et al.*, 1996). Strategies must interact, reinforcing and opposing each other. Therefore, this thesis makes a strong case on theoretical and empirical grounds for composite bundles of strategies as variables. In this context, the composite, low commitment *Cost Minimisation* strategy, was found to be negatively associated with insider ownership. The obvious explanation for this

association is the possible aversion of insiders to all retrenchment strategies, in the short run at least.

It has to be remembered that the FSU comprised a unique institutional environment, in which idiosyncratic governance characteristics involving dominant employee ownership have been suspected of promoting strategic inertia and of prevailing restructuring (Buck *et al.*, 2001). To some extent this is true for a modern Russia, since employee ownership is associated with less *CM* retrenchment. At the same time, the results here show no consistent association between the two high commitment composite strategies – *Traditional Social Welfare* and *Human Resource Investment* – and governance, represented by ownership variables and different legal structures. The absence of support for *TSW* and *HRI* effects of HRM and governance alignment on strategic outcomes may come as a surprise, although it is often difficult to specify what constitutes good alignment in research across firms and industries (Becker and Gerhart, 1996). Possibly, it could also be attributed to the strategic inertia associated with the influence of Russian employees.

6.2.2 Strategy – Performance

The second part of this research was focused on the examination of *Strategy – Performance* associations in Russian enterprises. As with the *Governance – Strategy*, an individual HRM-element approach was supplemented by the, arguably more appropriate, composite strategy analysis, extending the works of Buck *et al.* (2003) and Fey and Björkman (2001).

It was hypothesised in the main *Strategy – Performance* hypothesis (*Hypothesis 2*), that firms' strategies that promote employee welfare will be positively associated with improved corporate performance. The results for individual strategies, summarised in Table 15, are very mixed and do not permit one to confirm/reject this hypothesis straightaway, when for each performance indicator there are variables that support the association, and at the same time there are other variables that do not. As was noted, this

ambiguity may be attributable to the choice of regression parameters, taken from the one-year performance indicators of the ILO questionnaire. One cross-section of data may be insufficient to produce consistent patterns of results.

Bearing in mind the speculative nature of any discussion about causation in relation to employee-friendly strategies, some of the results show support for the argument of there being some possible improvement in the overall situation with corporate performance in Russia. For example, higher wages, as a proportion of production costs, are positively associated with a higher percentage of sales exported outside the CIS; a higher capacity utilisation rate is associated with greater spending on initial training and fewer workers on unpaid leave.

The association between higher wages and exports beyond the CIS may indicate that exported goods are of a better quality (what actually require better skills from workers) because of presumably tight economic competition and higher demands on outside markets. As a result, employees involved in the production of exported good are on average better paid. As was already argued, this result could indicate a need for manufacture retooling on production of those goods and services, that are in demand not only within the CIS, but outside also, though any drastic technological change requires substantial investments, and goes beyond the research interests of this welfare-focused study.

Positive relationships between the capacity utilisation rate and the initial form of training may indicate a rise in the demand for a qualified work force in expanding or emerging enterprises. This latter interpretation is also supported by an increase in training provided in association with an increase in the volume of production. However, other performance indicators – non-money wages, barter sales, exports within the CIS – are negatively associated with training provision. The situation with training variables might look rather misleading also because of the results from *Governance – Strategy* analysis, where training may be either significantly opposed by managers or have no association with workers' shareholdings. So it is possible that a positive association between an increase in the volume of production, capacity utilisation rate and training is only mechanical, since

workers must be trained if production is to be raised. Therefore, once more, one can only speculate on causality.

It is also worth mentioning that performance indicators, identified as negative for this study (e.g. the percentage of sales bartered or the percentage of wages paid non-monetarily), may, on the contrary, signalise positive economic performance, implying that enterprises are functioning and production continues within the limits imposed by an economy in crisis.

For the strategic clusters in relation to *Strategy – Performance*, the relationship between the use of HRM practices and firm performance did not hold across all three bundles of HRM practices (*Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment*). After transformation from a command-administrative system of management, typical of the FSU, to a capitalist society, Russian managers started to implement various Western high-commitment HRM practices. Fey and Björkman (2001) showed that *HRI* strategies in Russia were clearly associated with improved firm performance. Later, Buck *et al.* (2003) supported this result of Fey and Björkman (2001) of a positive association between *HRI* strategy and performance in their Ukrainian study. The results here go along with these two outcomes, confirming them in terms of two positive performance indicators – capacity utilisation and increase in production volume – and one negative performance indicator (bankruptcy threat). Here, the *HRI* strategy shows a positive and consistent association with performance, and supports *Hypothesis 8*, stating that firm performance is positively associated with new HRM investments. However, *HRI* is also significantly and negatively associated with sales exported outside the CIS, and this contradicts *Hypothesis 8*.

It was noted, that *HRI* strategies are positively associated with production measures of performance – capacity utilisation or increase in production – but not sales (in the form of exports). So, this recalls the experiences of centrally-planned Soviet enterprises, where strategies were focused on output increases rather then quality improvements, thus making goods and services non-competitive on foreign markets. Predominantly positive associations between *HRI* strategies and firms' performance may be interpreted as grounds

for optimism. This outcome is consistent with the possibility that *HRI* may be particularly suited to Russian managers and other employees, culturally and institutionally accustomed to high-commitment HRM, and hostile to cost minimisation. In fact, results for the *CM* bundle (uniformly insignificant) provide no support whatsoever to the supposition that *CM* has to be associated with worse performance, though *CM* strategy may have been opposed by all groups of insiders, as inconsistent with Russian culture and institutions.

As in the Fey and Björkman (2001) study, where the relationship between the use of composite HRM strategies and firm performance did not hold across all bundles introduced, our results for the other two high-commitment HRM strategies – *TSW* and *CM* – also did not produce any consistent outcomes. In particular, the non-significant association between *TSW* and firm performance (with one exception of significant association between the *TSW* and the proportion of wages paid non-monetarily, though positive) in our findings, contradicts the predictions made on the basis of the Western HRM theory, that this traditional form of welfare provision may result in improved performance.

Although this thesis has been restricted to HRM strategies, of course there may be a case for the State not contemplating further radical reform, allowing privatised firms to continue to make strategic choices (e.g. *HRI*) and let the market act as a referee in relation to their impact on performance. If this happens however, insider owned and controlled firms may have appropriate policies towards human capital, but may have to face more serious problems in relation to raising finance for investment in physical assets.

6.3 Novel Contribution of The Thesis

This research analyses Russian industrial firms in the year 2000, and focuses on their corporate governance, strategies in relation to employee welfare and on firm performance. After the break-up of the FSU in 1991, Russia came through a period of transitional policies, promoting global integration, and three waves of mass privatisation that lead to employee-owned businesses as the dominant form of governance in manufacturing

industry. For Russia, Ukraine and Belarus this has already been described by Filatotchev *et al.* (2000) and Hoskisson *et al.* (2000). To date, however, the relationship between HRM strategies and firm performance in Russia has been analysed only by Fey and Björkman (2001), who investigated 101 foreign-owned subsidiaries (Finnish, Swedish, US, German and British) in Russia. They found that greater HRM investments for managerial and non-managerial employees are positively related to firm performance. In addition to Fey and Björkman (2001), Buck *et al.* (2003) analysed the influence of governance forms on HRM strategies in Ukraine, and found that insider ownership in Ukrainian firms is positively associated with high-commitment *HRI* strategies, and negatively associated with low-commitment *CM* strategies. The latter, in turn, are associated with weaker firm performance.

This research extends the Fey and Björkman (2001) and Buck *et al.* (2003) analyses by: (a) supplementing the *Strategy – Performance* approach of Fey and Björkman (2001) with a consideration of associations between *Governance – Strategy – Performance* on a sample of indigenous industrial Russian firms; and (b) compared with Buck *et al.* (2003), by studying the most developed State, founded after the collapse of the Soviet Union (EBRD, 2001), thus allowing some generalisation of findings for the FSU as a whole.

As a result, the first stage of this research develops an HRM approach based on individual elements of HRM strategies, partly adopted from the Western literature for Russian firms, in order to state and test *Governance – Strategy – Performance* hypotheses. As a second stage, following the Western HRM literature on High Performance Work Organisations (Baron *et al.*, 1999; MacDuffie, 1995; Osterman, 1999), on transitional economies (e.g. see Spenner *et al.*, 1998, on Bulgarian SOEs research), and taking into account national culture and traditions of the FSU (in Ukraine, see Buck *et al.*, 2003), three strategic bundles, representing *Traditional Social Welfare*, *Cost Minimisation* and *Human Resource Investment* strategies were constructed for the examination of *Governance – Strategy – Performance* mechanisms. These bundles trace their origins. Thus, *TSW* was constructed according to the old Soviet-style template, involving costly resource commitments and amounting to paternalism by corporations. Being a rather unfashionable business strategy in Western firms (Wray, 1996), *TSW* is supplemented by two other, quite different

strategies – *CM* and *HRI*. Being a "hard" HRM strategy, *CM* involves downsizing, cuts in expenditures, short-term or contractual working schemes with lower wage rates, and other market-related work practices associated with cost minimisation. The less radical, "soft", *HRI* strategy proposes mutual high commitments from both the firm and employees, involving team-based compensation, training, development of human resources, etc. The adoption of these three strategic bundles (modified versions of those proposed by Buck et al., 2003), their associated methodologies and statistical techniques amount to novelty in their design and application to studies on Russia.

In addition, little emphasis in the Western *governance/strategy/performance* literature or in the literature on transitional economies has been placed on the penalties for poor performance, which can be more significant in a national economic crisis. In this context, it is actors' perceptions and expectations of negative phenomena (like the perceived bankruptcy threat or sales bartered) that may be expected to influence attitudes towards HRM policies. This study claims a novelty in the design and application of negative performance indicators, thus extending the view of Fey and Björkman (2001), who argue the case for subjective performance measures. As opposed to Buck *et al.* (2003), this study also uses legal forms as governance variables.

So, based on its developed methodology, this research has been able to identify core associations between *governance* and HRM *strategies*, and, in turn, the association of *strategies* with firm *performance*, through the empirical analysis of employee-related data for Russian enterprises.

As another novel feature, this research focuses on indigenous Russian privatised firms rather than foreign-owned subsidiaries only, thus giving a broader view of strategic response and inertia in the bulk of Russian firms, but providing complementary results.

6.4 SHORTCOMINGS OF THIS RESEARCH

As with any research, this study has a number of shortcomings and limitations. While the commentary has speculated on causation, the cross-sectional data of course do not allow conclusions on causality or examination of lagged effects (e.g. lagged influence of governance on strategies). This can only be established with time-series data collected for several years for a panel of firms (Becker and Huselid, 1998). The output of this thesis emphatically indicates that single cross-sections of data must be extended to identify causation. Of course time-series of data and panel data introduce more environmental instability over time, and panels are notoriously difficult to establish. (Subsequent surveys of Russian firms by the ILO have produced samples and results that are impossible to compare over time.) This all suggests an unavoidable trade-off, with the richness of data being sacrificed for methodologies designed to identify causation.

Another shortcoming relates to the necessarily limited nature of performance indicators available and appropriate in a volatile, inflationary Russian environment, with weak accounting conventions and enforcement. For example, no data was available on company profits, rates of return, etc. This shortcoming severely handicaps meaningful comparisons between HRM strategies and financial performance, as conventionally measured.

The estimation of associations between ownership, strategy and enterprise performance often involves the "implicit assumption that ownership structure is exogenous, i.e., not affected by performance itself" (Kuznetsov and Muravyev, 2001, p.18). However, once ownership is affected by enterprise performance (e.g. managers receive compensation in the form of equity), this assumption can be questioned. In early research it was usual to ignore this problem, only mentioning the possibility of reverse causality between "independent" and "dependent" variables (e.g. Demsetz and Lehn, 1985; McConell and Servaes, 1990) and to take all variables as exogenous. Subsequently, a number of authors have taken the issue into account when analysing the role of ownership structure (Brown and Earle, 2000; Earle, 1998) and in some cases, this has led to substantial changes in study results (Kuznetsov and Muravyev, 2001). As applied to ILO data and the results

obtained, there could be grounds for treating ownership variables as being partly endogenous. However, this again would demand more data.

Certainly, this analysis was limited to enterprises from four regions and cities only, although initially it was intended by the ILO to cover eight of them. The surveyed regions can be described as central and well-performing ones, when comparing with the data from the official Russian statistics, but the analysed sample of almost 300 firms restricts us to the comments/recommendation for these companies and regions only.

Finally, while the use of data collected and processed by professional staff of the ILO offered many advantages, it must be conceded that the lack of involvement in survey design and process led to sampling, questions and concepts in the questionnaire that could have been improved. This issue was addressed by using the three composite HRM bundles, rather than directly observable characteristics.

6.5 SUGGESTIONS FOR FUTURE RESEARCH

This work makes important contributions to the analysis of strategies of Russian firms in relation to HRM in the context of *Governance – Strategy – Performance* mechanisms, and reveals new areas for future research.

As was mentioned in the previous Section, panel studies can better address, though not irrefutably identify, causality in *Governance – Strategy – Performance* relations. To perform time-series analysis, new comparable data for a number of successive years is needed. A panel approach would give an opportunity to estimate cause-and-effect relations, to relate lagged enterprise performance to strategies applied in previous years, and to examine any lagged influence of governance on strategies.

The preceding theoretical discussion on high-commitment HRM bundles (*TSW*, *CM* and *TSW*) suggests that instead of using one single strategy, companies may usefully choose a sequence or mix of strategies in an experimental way. It was argued that in this case the

simultaneous use of both (or mixed) HRM strategies is more likely to be the source of sustainable competitive advantage. However, as long as it takes a number of years (and highly skilled management) to fully implement one strategy, before changing to another one, time-series of data could provide an interesting ground for studying the specified HRM strategies in a sequence or mix.

Although the choice of statistical approaches was justified for this research, rejecting other approaches and highlighting their limitations, it nevertheless could be useful to employ Structural Equation Modelling (SEM) techniques for the examination of relations between governance, HRM strategies, and firm performance. Being applied cautiously, SEM can offer an advance in comparison with multivariate regression analysis by providing an opportunity to study simultaneous inter-dependencies between governance, strategy and performance, though, of cause, some causality problems remain and the data demands of SEM are unrealistic in the Russian context.

Finally, it also seems possible to extend this research beyond Russia, one of the most developed independent States emerged from the FSU. While, Ukraine has already been studied by Buck *et al.* (2003), other transition economies (particularly China) could be compared to judge the possible culture and institution-specific nature of the results reported here.

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Appendix I

Russian Questionnaire

Question 1: Industrial Sector

1	Basic metallurgy	8	Chemical
2	Precious metallurgy	9	Wood processing
3	Engineering	10	Construction materials
4	Food processing	11	Medicine
5	Textile	12	Paper production
6	Clothing	13	Leather processing
7	Shoes		

Question 2: Region

1	Moscow	5	Ivanovo
2	Moscow region	6	Tatarstan
3	St. Petersburg	7	Vladimir
4	Nizhni Novgorod	8	Chelyabinsk

Question 3: Property Form / 2000

1	State, municipal, leasehold	4	Open joint stock
2	Partnership/production cooperative	5	Private (individual)
		6	Public organisation
3	Closed joint stock	7	Other

Question 4: Establishment Type

1	Independent	2	Part of larger enterprise	3	Other

Question 5: Percentage of Shares

	June, 2000
Workers' and Managers'	5.1
Workers'	5.2
State's	5.3
Foreign	5.4

Question 6: Percentage of Sales

	1999
Exported Within the CIS	6.1
Exported Outside the CIS	6.2
Bartered	6.3

Question 7: Percentage of Shares of Production Costs

	1999
Wage Share	7.1
Social Cost Share	7.2
Training Share	73

Question 8: Total Number of Workers / June 2000

Question 9: Number of Workers on Administrative Leave

	June 2000
Unpaid	9.1
Partially Paid	9.2
Full Paid	9.3

Question 10: Turnover, Number of Workers / June 1999 – June 2000

	Total	Resigned	Dismissed
Number of Workers	10.1	10.2	10.3

Questions 11-13: Earnings, in 000 Roubles / June 2000

	Number of Employees	Average Wage	Bonuses	Benefits
Managers	11.1	11.2	11.3	11.4
Skilled	12.1	12.2	12.3	12.4
Unskilled	13.1	13.2	13.3	13.4
All	14.1	14.2	14.3	14.4

Question 15: Foreign Investments in Enterprise

1 Yes 2 No 3 Do not know

Question 16: Initial Training

1 Yes 2 No 3 Do not know

Question 17: Retraining to Improve Job Performance

1 Yes 2 No 3 Do not know

Question 18: Providing Training to Upgrade

1 Yes 2 No 3 Do not know

Question 19: Change in Period Training Program / June 1999 – June 2000

1 Decreased 2 No change 3 Increased

Question 20: Paying for Special Training Institute / June 1999 – June 2000

1 Yes, its own institute 5 Yes, grants

2 Yes, transfer funds to an institute 6 Other

4 Yes, each student 7 Not paying

Question 21: Is Paying Practice Going on Now?

1 Yes 2 No 3 Do not know

Question 22: Planning to Cut Financing the Training Institute

1 Yes 2 No 3 Do not know

Question 23: Change in Volume of Production

1 Increase 2 No change 3 Decrease

Question 24: Effect of Product Range Change on Employment

1 Increase 3 Decrease

2 No change 4 Do not know

Question 25: Effect of Technological Change on Employment

1 Increase 3 Decrease

2 No change 4 Do not know

Question 26: Effect of work organisation change on employment

1 Increase 3 Decrease

2 No change 4 Do not know

Question 27: Capacity Utilisation, % / June 2000

Question 28: Main Criteria of Wage Determination

1 Performance of establishment as a whole 4 Minimum Wage Law

2 Work brigade/unit performance 5 Other

3 Individual performance

Question 29: Percentage of Workers Paid Non-monetarily

Question 30: Percentage of Wages Paid Non-monetarily

	2000
Workers	30.1
Workers' and Managers'	30.2

Question 31: Percentage of Wage Not Paid on Time

Question 32: Operating a Profit Sharing System / June 1999 – June 2000

1 Yes 2 No 3 Do not know

Question 33: Remuneration System / Employees

1 Basic wage
2 Basic wage with individual bonuses
3 Basic wage with monthly bonuses
4 Basic wage with quarterly bonuses
5 Other

Questions 34-35: Benefits

	Administrative Workers	Regular Workers
Paid Vacation	34.1	35.1
Additional Vacation	34.2	35.2
Rest Houses	34.3	35.3
Sickness Benefit	34.4	35.4
Paid Health Services	34.5	35.5
Subsidised Rent	34.6	35.6
Subsidies for Kindergartens	34.7	35.7
Bonuses	34.8	35.8
Profit Sharing	34.9	35.9
Loans	34.10	35.10
Retiring Assistance	34.11	35.11
Supplementary Pension	34.12	35.12
Possibility for Training	34.13	35.13
Subsidy for Benefit for Meal	34.14	35.14
Subsidised Consumer Goods	34.15	35.15
Transport Subsidies	34.16	35.16
Unpaid Shares	34.17	35.17

1 Yes 3 Occasionally 5 Do not know

2 No 4 N/A

Question 36: Main New Social Benefit Added / June 1999 – June 2000

0	None	7	Social insurance
1	Subsidised catering	8	Subsidised kindergarten
2	Subsidised transport	9	Vouchers, subsidised prices
3	Subsidised housing	10	Profit sharing
4	Payment for additional vacation	11	Financial assistance
5	Medical service	12	Other
6	Medical insurance		

Question 37: Main Social Benefit Excluded / June 1999 – June 2000

0	None	7	Social insurance
1	Subsidised catering	8	Subsidised kindergarten
2	Subsidised transport	9	Vouchers, subsidised prices
3	Subsidised housing	10	Profit sharing
4	Payment for additional vacation	11	Financial assistance
5	Medical service	12	Other
6	Medical insurance		

Question 38: Maintaining Social Facilities

1 Yes 2 No

Question 39: Social Facilities Passed to Local Authorities / June 1999 – June 2000

1 Yes 2 No

Question 40: Providing Service Housing

1 Yes 2 No 3 Do not know

Question 41: Going Bankrupt in the Next 12 Months

1	Yes	4	No
2	Probably yes	5	Do not know
3	Probably no		

Appendix II

Cluster Analysis

Cluster analysis seeks to identify homogenous subsets of cases in a population, i.e. cluster analysis seeks to identify a set of groups, which both minimise within-group variation and maximise between-group variation (Garson, 2001).

The problem, solved by means of cluster analysis is in the distribution of the set of data I into m clusters (subsets of data) $I_1, I_2, \ldots, I_m$ so that each variable was belonging to one particular construct only. The idea is to determine whether or not the information can be summarised into a smaller set of constructs and to put alike objects into one clusters and diverse into different ones. The solution to the problem of cluster analysis lies in the distribution that matches to some criterion of optimality that consists of an optimal *distance measure* and a *measure of similarity.*

The *distance measure* is an Euclidian distance between two points x and y calculated with the following formula:

$$d^2 = \sum_{i=1}^{m} (x_i - y_i)^2$$

It is also known that object with a description X is *similar* to the object from some set $Y(y_i)$ if a mean squared distance between point x and any point from a set Y is small. In other words, the point x is close to the set Y if $d_1^2(x,Y) = \frac{1}{n_y}\sum_{i=1}^{n_y} d^2(x,y_i)$ is small.

To be able to compare two different sets, it is necessary to estimate a mean distance between a pair of points, each being taken from a particular set. Thus for sets X and Y the distance $d(X,Y)$ is estimated with $d_2^2(X,Y) = \frac{1}{n_x n_y}\sum_{i=1}^{n_x}\sum_{j=1}^{n_y} d^2(x_i,y_j)$

To estimate a density among points inside the sets, the following measure is used:

$$d_3^2(X,Y) = \frac{1}{n_x(n_x-1)} \sum_{i=1}^{n_x-1} \sum_{j=i+1}^{n_x} d^2(x_i, y_j)$$

The smaller the result is, the closer are the points inside the set.

In general, the idea of this approach is in transformation of a space of descriptions D into a space D^*, where all points from one set are allocated close to each other, and points from different sets are distanced.

To solve the problem of cluster analysis, it is necessary to define formally what is included into the term of *similarity* and into the term of *difference*. This solution lies in the distribution where the distance between x_i and x_j is small enough in one cluster, and the distance between x_i and x_j is rather big in different clusters. For these purposes it is possible to analyse any function, that satisfies to the following conditions (not only the Euclidian distance).

The *distance* conditions:

Any nonnegative real function $d(x_i,x_j)$ is called the *distance function* (or metric) if:

a) $d(x_i,x_j) \geq 0$ for any x_i and x_j;

b) $d(x_i,x_j) = 0$ if and only if $x_i = x_j$;

c) $d(x_i,x_j) = d(x_j,x_i)$;

d) $d(x_i,x_k) \leq d(x_i,x_j) + d(x_j,x_k)$ for any x_i, x_j and x_k.

The *measure of similarity*:

Any nonnegative real function $S(x_i,x_j)$ is called the *measure of similarity* if:

a) $0 \leq S(x_i,x_j) \leq 1$ for $x_i \neq x_j$;

b) $S(x_i,x_i) = 1$;

c) $S(x_i,x_j) = S(x_j,x_i)$.

A pair of *measures of similarity* organise a similarity matrix:

$$S=\begin{bmatrix} 1 & S_{12} & \cdots & S_{1n} \\ S_{21} & 1 & \cdots & S_{2n} \\ \vdots & \vdots & \ddots & \vdots \\ S_{n1} & S_{n2} & \cdots & 1 \end{bmatrix}$$, where the term S_{ij} is called a coefficient of similarity.

In statistical analysis the measure of linear similarity is used. It is calculated by the formula:

$$r_{ij}=\frac{\sum_{k=1}^{n} x_{ki}x_{kj}}{\left[\sum_{k=1}^{n} x_{ki}^2\right]\left[\sum_{k=1}^{n} x_{kj}^2\right]^{1/2}}$$ and is called a coefficient of correlation.

The coefficient of correlation $r_{ij}=1$ if and only if $x_i=kx_j$, where k is nonnegative.